Technical Bulletin 2021/1

Technical developments and emerging risks from January to March 2021

Prepared for appointed auditors and audited bodies in all sectors

24 March 2021

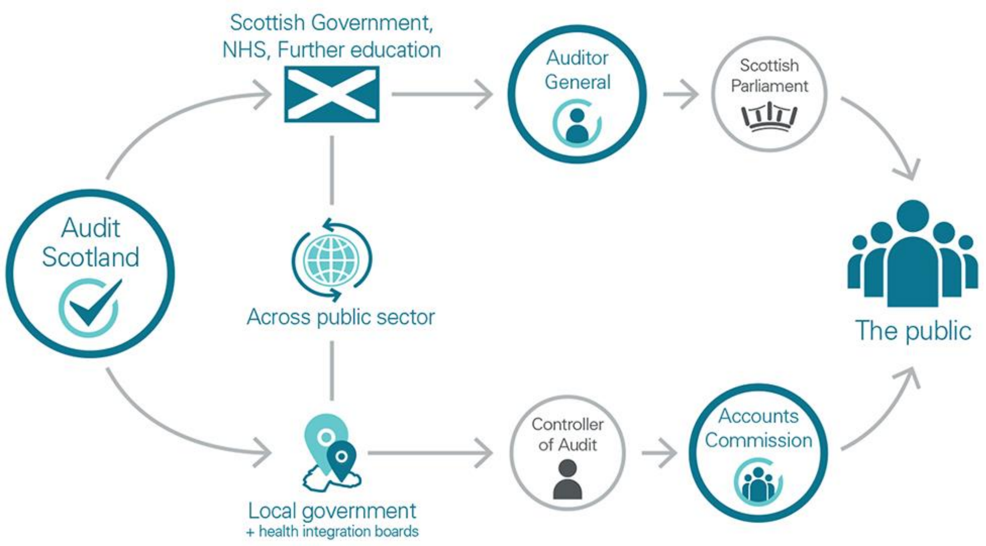
Who we are

The Auditor General, the Accounts Commission and Audit Scotland work together to deliver public audit in Scotland:

- The Auditor General is an independent crown appointment, made on the recommendation of the Scottish Parliament, to audit the Scottish Government, NHS and other bodies and report to Parliament on their financial health and performance.

- The Accounts Commission is an independent public body appointed by Scottish ministers to hold local government to account. The Controller of Audit is an independent post established by statute, with powers to report directly to the Commission on the audit of local government.

- Audit Scotland is governed by a board, consisting of the Auditor General, the chair of the Accounts Commission, a non-executive board chair, and two non-executive members appointed by the Scottish Commission for Public Audit, a commission of the Scottish Parliament.



About us

Our vision is to be a world-class audit organisation that improves the use of public money.

Through our work for the Auditor General and the Accounts Commission, we provide independent assurance to the people of Scotland that public money is spent properly and provides value. We aim to achieve this by:

- carrying out relevant and timely audits of the way the public sector manages and spends money

- reporting our findings and conclusions in public

- identifying risks, making clear and relevant recommendations.

Contents

Introduction

Purpose

Technical Bulletins provide information on developments and guidance on emerging risks

1. The purpose of Technical Bulletins from Audit Scotland's Professional Support is to provide auditors appointed by the Auditor General and Accounts Commission with:

- information on the main technical developments in each sector during the quarter
- information on professional matters during the quarter that are expected to have applicability to the public sector
- guidance on any emerging risks identified in the quarter.

2. Appointed auditors are required to pay due regard to Technical Bulletins. The information on technical developments is aimed at highlighting the key points that Professional Support considers auditors in the Scottish public sector require to be aware of. It may still be necessary for auditors to read the source material if greater detail is required. These can be accessed by using the hyperlinks. They are also available from the Technical Reference Library maintained by Professional Support.

3. The actions by auditors recommended by Professional Support in respect of each item are highlighted in red and are also summarised at the end of each section.

4. Technical Bulletins are also published on the Audit Scotland website and therefore are available to audited bodies and other stakeholders. However, hyperlinks in this bulletin indicated with an asterisk link to documents on the Technical Reference Library and therefore are active only for auditors.

Highlights summary

5. Professional Support draws attention in the following table to certain items in this Technical Bulletin:

Highlights summary		
Professional Support has published 2020/21 assurance protocols for LGPS and IJBs [see paragraph 7]	Professional Support has published a GPN on disclosing judgements and estimates [see paragraph 9]	Regulations have been issued to permit the deferral of loans fund repayments [see paragraph 17]
The Scottish Government has issued new statutory guidance on the use of capital receipts [see paragraph 21]	CIPFA has issued consultation papers on the prudential and treasury management codes [see paragraphs 31 and 34]	Professional Support has published guidance on risks of misstatement in 2020/21 annual accounts [see paragraphs 41 and 62]
Professional Support has published model Independent Audits Reports for 2020/21 [see paragraphs 45 and 64]	Treasury has issued the 2020/21 FReM and an addendum [see paragraphs 51 and 52]	The SG has issued guidance on 2020/21 health board accounts [see paragraph 70]
The UK Government has issued proposals related to reviews of the audit profession [see paragraph 75]	The ICAEW has issued a guide on the impact of COVID-19 on determining materiality [see paragraph 77]	The FRC has issued proposals to revise standards on audit quality [see paragraph 81]

Contact point

6. The main contact point for this Technical Bulletin is Paul O'Brien, Senior Manager (Professional Support) – pobrien@audit-scotland.gov.uk.

Feedback on this Technical Bulletin is welcome

Section 1

Local government sector

Auditing developments

Assurance protocols for 2020/21

7. Professional Support has published two protocols to provide agreed frameworks for auditors to seek and provide certain assurances from auditors of other public bodies. The protocols are summarised in the following table:

Protocol subject	Nature of assurances
Local Government Pension Scheme (LGPS)	LGPS pension fund auditors request assurances from employer body auditors in respect of pension contributions payable by the employer body to the pension fund. Employer body auditors request assurances from pension fund auditors in respect of information provided by the pension fund to the actuary in relation to their reports on employer bodies.
Integration joint boards (IJBs)	IJB auditors request assurances from the auditors of the constituent authorities regarding information not held by the IJB.

8. Auditors may judge that it is not necessary to request any assurances from other auditors. However, where assurances are judged to be appropriate, these protocols set out the potential range of assurances.

Auditor action
Auditors should use the protocols when seeking assurance in these areas

Financial statements developments

Good practice in disclosing judgements and estimates

9. Professional Support has published a Good Practice Note (GPN) following a review of the disclosures of judgements on the application of accounting policies (judgements) and assumptions about the future and other sources of estimation uncertainty (estimates) in local authorities' 2019/20 financial statements.

10. These disclosures were chosen for a good practice review because of their fundamental importance in understanding the financial statements, along with indications that the quality of the disclosures was variable. Good practice is illustrated, where possible, using examples taken from the 2019/20 financial statements of the councils reviewed. The GPN also includes points for local authorities to consider in striving to achieve good practice.

11. The review was carried out by a team with knowledge of the relevant financial reporting framework. However, the team does not have a detailed understanding of each authority's particular circumstances or the specific underlying transactions.

12. Local government bodies are encouraged to use the findings in this GPN to assess and enhance their own disclosures in 2020/21.

Auditor action
Auditors should encourage bodies to use the GPN

2020/21 disclosure checklist

13. The Chartered Institute of Public Finance and Accountancy (CIPFA) has issued a disclosure checklist* for the 2020/21 annual accounts. It is intended for use as an aide-memoire to assist in meeting the requirements of the Code of Practice on Local Authority Accounting in the United Kingdom (the accounting code).

The checklist is an aide-memoire

14. The checklist is in the form of a series of questions and the implications of the answers are set out in the following table:

Answer	Implication
Yes	The accounting code is being complied with.
No	A justification for departing from the accounting code should be given. For example, a legitimate justification may be that the information resulting from that disclosure is not material.

15. When evaluating whether the accounting code's disclosure requirements have been met, auditors should:

- request that the body completes the 2020/21 disclosure checklist
- investigate the reasons for any non-compliance that the checklist highlights
- evaluate whether the body's responses in the checklist are consistent with auditor's knowledge.

Auditor action
Auditors should request completion of the checklist

16. Where the body declines to complete the checklist, auditors should establish the alternative means by which it satisfies itself regarding the completeness of disclosures, and evaluate the adequacy of the arrangements. Where the arrangements are not adequate, auditors should consider completing the checklist as part of their audit procedures.

Regulations on deferring loans fund repayments

17. The Local Authority (Capital Finance and Accounting)(Scotland)(Coronavirus) Amendment Regulations 2021 have been issued to allow a local authority to defer loans fund repayments in either 2020/21 or 2021/22.

Loans fund repayments can be deferred in 2020/21 or 2021/22

18. Regulation 3 of the amendment regulations adds Regulation 14A to The Local Authority (Capital Finance and Accounting) (Scotland) Regulations 2016 (the 2016 regulations) to allow this deferral. However, if a local authority has decided since 31 March 2020 to increase an existing repayment, the increased element is not available for deferral.

19. Any deferred repayment is to be repaid within the shorter of the remaining period of the loans fund advance to which that deferral relates or 20 years. However, the local authority may use its powers under regulation 14(2) of the 2016 regulations to vary the repayment period.

20. In addition, Regulation 6 of the amendment regulations amends Regulation 13 of the 2016 regulations to allow the existing repayment provisions to be replaced with statutory guidance from 1 April 2022.

New statutory guidance on use of capital receipts

21. The Scottish Government has issued Finance Circular 2/2021 which contain statutory guidance in respect of the use of capital receipts to fund the financial impact of COVID-19. Key aspects of the guidance are summarised in the following table:

Aspect	Provisions in guidance
Qualifying expenditure	The statutory guidance does not define qualifying expenditure. The local authority will be required to demonstrate, by reporting to full council, how the capital receipts are to be used to fund the financial impact of COVID-19. Full council will be required to approve the use.
Qualifying capital receipts	Only capital receipts received in 2020/21 or 2021/22 can be applied. The decision on use is required to be made in the year the capital receipt is recognised.
Accounting treatment	The capital receipt requires to be transferred as a statutory adjustment to the Capital Grant and Receipts Unapplied Account in the year of receipt. Capital receipts so transferred in 2020/21 can be applied in that year or in 2021/22. Any unused capital receipts at 21 March 2022 will be transferred to the Capital Fund.
Disclosure requirements	The reason for each transfer of capital receipts from the Capital Grants and Receipts Unapplied Account to the General Fund or Capital Fund should be disclosed. All the elements of the balance on the Capital Grants and Receipts Unapplied Account are to be disclosed separately.

Pension fund illustrative accounts for 2020/21

22. CIPFA has issued revised illustrative financial statements* for LGPS pension funds. They set out a fund account and a net assets statement, as well as information to be disclosed in the notes, that comply with the 2020/21 accounting code. The publication also includes a disclosure checklist that identifies the accounting code's requirements in relation to pension funds.

23. The most significant changes arise from amendments to section 6.5 of the 2020/21 accounting code in respect of:

- the removal of the requirement to analyse assets between quoted/unquoted and UK/ overseas
- the revised analysis requirement for pooled investment holdings (Note 14)
- more detailed disclosure requirements in respect of investment management fees (Note 11a).

Changes to 2020/21 annual accounts deadlines

24. The Local Authority Accounts (Scotland) Regulations 2014 (2014 regulations) have been amended in respect of approval and publication dates for the 2020/21 annual accounts. Regulation 5 of The Local Authority (Capital Finance and Accounting)(Scotland)(Coronavirus) Amendment Regulations 2021 amends the dates as set out in the following table:

Action	Normal date	2020/21 date
Approval to sign off accounts	30 September	31 October
Publication of accounts	31 October	15 November

Statutory other information

Bulletin on 2020/21 Annual Governance Statements

25. CIPFA has issued a bulletin on the impact on governance in local government in 2020/21 of COVID-19 and the introduction on a 'shadow' basis of the Financial Management (FM) Code. The main issues covered in the bulletin are summarised in the following table:

Area	Summary of main issues
COVID-19 impact	• Identify changes made to governance arrangements to adapt to COVID-19. • Explain in the Annual Governance Statement (AGS) the significant adaptations to governance arrangements. • Disclose in the AGS any limitation of scope on the opinion provided by the Head of Internal Audit on governance, risk management and internal control. • Report a clear conclusion in the AGS on whether the arrangements are fit for purpose. • Include in the action plan any actions needed to restore aspects of governance arrangements.
Introduction of FM Code	• Assess the extent to which the body's financial management arrangements comply with the principles in the FM Code. • Report an overall conclusion in the AGS of the above assessment and explain how it was carried out. • Include outstanding matters or areas for improvement in the action plan.

26. Appendix A to the bulletin provides a summary of the key content of an AGS for 2020/21.

Grant claims and returns

Technical Guidance Notes

27. Professional Support has published a number of Technical Guidance Notes (TGNs) on certifying 2020/21 grant claims and returns. The TGNs are provided with supporting material to auditors on SharePoint* and are also the Audit Scotland website. They are summarised in the following table:

TGN	Claim
TGN/GEN/21	General guidance on all claims
TGN/EMA/21	Education Maintenance Allowances
TGN/BEL/21	Bellwin Scheme for Special Financial Assistance for Local Authorities

Housing benefits

28. The Department for Work and Pensions (DWP) has issued:

- the housing benefit (HB) subsidy claim form and notes for its completion for 2020/21
- Module 2* of the Housing Benefit Assurance Process (HBAP) approach to the certification of HB subsidy claims for 2020/21. Module 2 contains a checklist to help ensure the correct benefit parameters are used.

Non-domestic rates

29. The Scottish Government has issued statutory guidance with Finance Circular 3/2021 in respect of discretionary relief from non-domestic rates for sports clubs. Local authorities are required to have regard to this guidance when choosing to award sports relief from 2021/22. The guidance advises authorities to consider targeting sports relief at organisations that provide facilities for recreation and:

- are set up with a formal constitution or governing document
- are open to the whole community (taking into account reasonable exclusions)

- have affordable membership and/or participation fees
- are organised on an amateur basis
- are managed by 'fit and proper persons'.

30. Local authorities can adopt additional specifications or local policies if they wish to do so.

Wider audit scope developments

Proposed changes to prudential code

31. CIPFA has issued a consultation paper which proposes changes to the Prudential Code for Capital Finance in Local Authorities (the prudential code). The prudential code provides a framework for local authorities to ensure their capital investment plans are affordable, prudent and sustainable.

32. Since the current edition was published in 2017, local authorities in the UK have increasingly invested in commercial properties. Many of the proposals are intended to strengthen the code's provisions in that area. The proposals are summarised in the following table:

Paras	Area	Summary of proposals
1	Augmenting the objectives of the code	Option appraisal should ensure that capital expenditure is sustainable in accordance with the corporate objectives of the authority. Capital expenditure and investment plans should be proportionate. Any commercial investment undertaken should be consistent with statutory provisions, proportionate to service budgets and consistent with effective treasury management practice.
23	Strengthening the provisions related to commercial activity	The capital strategy should include: • an assessment of affordability of commercial activities • details of the risks involved.
45	Strengthening the provisions related to borrowing in advance of need	Authorities must not borrow more than or in advance of their needs primarily (rather than the current 'purely') in order to profit from the investment of the extra sums borrowed. An explicit statement that authorities must not borrow to fund primarily yield-generating investments.
78 - 81	New prudential indicators for affordability	External debt to net revenue stream ratio - intended to ensure that the amount of debt incurred is proportionate to a local authority's total service expenditure on a taxation basis.
82 - 85		Net income from commercial and service investments to net revenue stream - considers an authority' exposure to risk from commercial and service investment income.
90 - 92		Liability benchmark - to measure borrowing levels and the profile of debt over time.

33. Comments on the proposals should be sent to Policy.Technical@cipfa.org by 12 April 2021.

Proposed changes to treasury management code

34. CIPFA has issued a consultation paper which proposes changes to the Treasury Management in the Public Services Code of Practice (the TM code). The proposed changes to the treasury management practices (TMPs) set out in the TM code are summarised in the following table:

TMP	Area	Summary of proposal
10	Training and qualification	• Amendments to highlight the importance of all treasury management staff and members having the required skills and knowledge to be able to undertake their duties and responsibilities. • Bodies required to explicitly document a formal and comprehensive knowledge and skills schedule. • Bodies should consider how to assess whether treasury management staff and members have the required knowledge and skills to undertake their roles and whether they have been able to maintain those skills and keep them up to date. • Guidance to specify key competencies for treasury management roles (example in Annex 1).
12	Corporate governance	• Guidance to recommend that decisions and strategies for more complex treasury management functions should be reviewed by a dedicated committee.
13	Environment, social and governance	• A new TMP on the arrangements for the identification, management and control of environmental and social risks.

35. Comments on the proposals should be sent to Policy.Technical@cipfa.org by 12 April 2021.

Section 106 bodies

Reducing the number of charities accounts

36. Professional Support has issued a briefing for auditors* to encourage a reduction in the number of sets of accounts of registered charities that fall within the scope of section 106 of the Local Government (Scotland) Act 1973 (section 106 charities). The briefing provides information on:

- the number of section 106 charities administered by each council in 2019/20
- the number of related sets of accounts.

Auditor action
Auditors should encourage councils to reduce their number of section 106 charities

37. Most councils continue to administer multiple section 106 charities; ten councils administer more than five. In order to reduce the number of statements of account that require to be audited in 2020/21, auditors should strongly encourage councils with multiple charities to:

- reorganise their charities through merging or winding them up, particularly when they appear to be failing to meet their charitable aims (e.g. by not disbursing funds)
- consider appointing an external trustee as this would remove the charity from the scope of section 106.

38. In the meantime, there is scope for connected charities to prepare a single set of accounts. Connected charities have ‘common or related purposes, or charities which have common control or unity of administration’. In Professional Support’s view, the definition is met for section 106 charities administered by the same council even where trustees differ. However, in 2019/20

- five councils made only partial use of the connected charities provisions and produced 19 sets of accounts between them
- six councils made no use of the provisions and produced 20 sets of accounts.

Auditor action
Auditors should encourage councils to fully use connected charities provisions

39. Auditors should strongly encourage councils to make full use of the connected charities provisions in 2020/21.

Summary of auditor actions in this section

Paragraphs	Auditor actions
7-8	Use the protocols when seeking assurance over the LGPS and IJBs
9-12	Encourage audited bodies to make use of the GPN when disclosing judgements and estimates
13-16	Request completion of the disclosure checklist and investigate reasons for non-compliance
34-37	Encourage councils to reduce their number of section 106 charities and make full use of the connected charities provisions

Contact point for this section

40. The contact point for this section of the Technical Bulletin is Paul O'Brien, Senior Manager (Professional Support) - pobrien@audit-scotland.gov.uk.

Section 2

Central government sector

Auditing developments

Technical Guidance Note on risks of misstatement in 2020/21

41. Professional Support has published Technical Guidance Note (TGN) 2021/1 to provide auditors with guidance on risks of misstatement in the 2020/21 annual report and accounts of central government bodies. The TGN is available with supporting material to auditors on SharePoint* and is also freely available from the Audit Scotland website.

Auditor action
Auditors should pay due regard to TGN 2021/1

42. The TGN is intended to inform auditors' judgement when identifying and assessing the risks of material misstatement in 2020/21. The TGN supplements the Code of Audit Practice and auditors are expected to pay it due regard and use it as a primary reference source when performing 2020/21 audits.

43. The TGN structure comprises a number of modules as summarised in the following table:

Module	Risks of misstatement area	Purpose
Overview	Areas that are pervasive to the financial statements as a whole	Explains the appropriate related accounting treatment and sets out the action auditors should undertake to evaluate whether the body has followed the required treatment
1 – 8	Specific classes of transactions, balances and disclosures in the financial statements.	
9	Irregularities in expenditure and income	Explains the requirements and sets out the action auditors should undertake
10	Audited part of the Remuneration and Staff Report	
11	Statutory Other Information (e.g. Performance Report and Governance Statement)	Sets out the procedures for considering the Statutory Other Information
12	Charitable NDPBs	Provides guidance on the application of the above modules to charitable NDPBs

44. The risks of misstatement for 2020/21 have been updated to reflect new requirements and risks which emerged during the 2019/20 audits that remain applicable.

2020/21 model Independent Auditor's Reports

45. Professional Support has published TGN 2021/4(CG to provide auditors with the model Independent Auditor's Reports (IARs) which should be used for the 2020/21 annual report and accounts. Auditors are required by the Code of Audit Practice to prepare their IARs in accordance with this TGN. The TGN is available with supporting material to auditors on SharePoint* and is also freely available from the Audit Scotland website.

Auditor action
Auditors should use this TGN when reporting the audit of the 2020/21 annual accounts and complete the checklist

46. The model IARs set out in Appendices 1 to 4 of the TGN have been tailored to reflect central government legislation and augmented by the reporting requirements of the Auditor General.

47. There are a number of changes to the model IARs as a result of revised versions of international standards on auditing (ISAs) applying in 2020/21 and other changes to the guidance. These are summarised in the following table:

Reason for change	Nature of change
Change to models arising from revised ISAs	• The assurance on the going concern basis of accounting is now in the form of a positive statement (rather than reported by exception). • The explanation of the extent to which the audit is considered capable of detecting irregularities has been revised to give greater focus to non-compliance with laws and regulations. • The opinions on the Remuneration and Staff Report and Statutory Other Information are now in separate parts of the model IARs, with the description of the auditor's responsibilities for Statutory Other information clarified and moved to the latter part. • There are some additional changes in the model for Scottish Water.
Other changes to models	• As Scottish Canals is classified as an NDPB for 2020/21, a separate model is no longer required.
Changes in guidance	• Additional emphasis has been added of the requirement to discuss any modifications or additions to the model IAR with Professional Support, including any Emphasis of Matter paragraph. • Wording has been specified for use where auditors judge an Emphasis of Matter paragraph is appropriate where the declaration of a 'material valuation uncertainty' has been disclosed'.

48. The TGN also provides guidance on the amendments that require to, or may, be made to the wording in the models in the form of auditor actions. Auditors should complete for each report the checklist at Appendix 6 which provides a list of those auditor actions.

49. Any proposed modifications to any audit opinion or conclusion, or the inclusion of Emphasis of Matter or Other Matter paragraphs, should be discussed with Professional Support in advance of finalising the report.

2020/21 GBS account information

50. Professional Support will obtain information on account balances at 31 March 2021 for central government bodies from the Government Banking Service (GBS) and distribute them to relevant auditors. The GBS has confirmed that the arrangements for obtaining 2020/21 account balances are unchanged.

Annual report and accounts developments

Revised 2020/21 FReM

51. HM Treasury has issued a revised version of the 2020/21 Government Financial Reporting Manual (the FReM). Changes from the original version referred to in Technical Bulletin 2020/1 (paragraph 43) are as follows:

- A new part E has been added to provide further guidance on pensions accounting and on whole of government accounts.
- Additional guidance has been included throughout chapter 2, particularly paragraphs 2.6.8 to 2.6.13 on the application of materiality to the performance and accountability reports, to help decide what to include in these reports and explain the importance of linkages.
- An adaptation to IFRS 9 has been added (table at paragraph 8.2.2.) to clarify that financial instrument balances within a group are not covered by the exception from recognising expected credit losses.

Addendum to 2020/21 FReM

52. Treasury has issued an Addendum to set out the minimum requirements of the 2020/21 FReM. In response to the continuing impact of COVID 19, the minimum requirements are largely the same as for 2019/20.

FReM addendum sets out minimum requirements for 2020/21

53. The addendum permits, but does not require, bodies to omit the performance analysis section from the Performance Report. Where relevant performance information has already been published elsewhere, bodies are encouraged to refer to the relevant publication.

54. Where unaudited information otherwise required to be included in the Accountability Report is already published elsewhere, bodies are permitted to refer to the relevant publication rather than including the information in their Accountability Report.

2021/22 FReM

55. Treasury has issued the 2021/22 FReM. This is the first edition of the FReM to apply UK (rather than EU) endorsed IFRS and interpretations. It applies those standards in effect for accounting periods commencing on or before 1 January 2021, except for IFRS 16 Leases which is deferred until 2022/23.

56. The main changes in the 2021/22 edition of the FReM apply to the Remuneration and Staff Report and relate to:

- additional guidance and reporting requirements for the single total figure of remuneration table (paragraphs 6.5.8 e) to 6.5.15)
- revised disclosures for fair pay (6.5.19 to 6.5.24).

Main changes are to Remuneration and Staff Report

57. The changes in respect of the single figure of remuneration disclosures are summarised in the following table:

Area	Disclosure
Additional columns	New option for the body to include additional columns setting out other items of remuneration.
Comparative amounts	New requirement to disclose equivalent amounts for the prior year.
Recovery or withholdings	New guidance on how to treat any remuneration in the prior year that is the subject of a recovery or withholding. A new requirement to disclose an explanation for the recovery or withholding and the basis of the calculation.
Prior year estimates	Guidance that any estimates in the prior year should be replaced with actual amounts and new requirements for related disclosures.
Non-cash benefits	New requirement to disclose types and value of benefits.
Performance pay and bonus	New requirement to disclose how the performance pay and bonus award was determined.

58. The previous fair pay disclosures have been revised. As the revisions are based on regulations issued under the Companies Act, the requirement for fair pay disclosures will apply to Scottish bodies from 2021/22. They are summarised in the following table:

Area	Requirement
Remuneration change from prior year	• The percentage change in respect of the highest paid director. • The average percentage change for all employees. • Comparative amounts for 2020/21 encouraged if available.
Pay ratio information for	• 25th, 50th and 75th percentile pay ratio. • Comparative information for 2020/21 for the 50th percentile and, where available for 25th and 75th. • Total pay and benefits, and salary separately, for the 25th, 50th and 75th percentile. • Salary component of total pay and benefits 75th percentile pay ratio.

Area	Requirement
Summary narrative	• An explanation of whether movement in the ratios is attributable to a change in the highest paid director's remuneration or the employees, or a change in the body's employment models. • Trends in the median pay ratio. • An explanation of whether the body believes that the median pay ratio reflects the pay, rewards and progression policy for employees as a whole.

Revised 2020/21 discount rate

59. Treasury has issued a revised PES(2020)12* on discount rates for general provisions, post-employment benefits liabilities, and financial instruments as at 31 March 2021. The revised paper replaces the original explained in Technical Bulletin 2020/4 (paragraph 56).

60. The revision updates the real post-employment discount rate from minus 1.03% to minus 0.95%.

Summary of auditor actions in this section

Paragraphs	Auditor actions
39-42	Pay due regard to TGN 2021/1 when performing the audit of 2020/21 annual report and accounts
43-47	Use TGN 2021/4(CG) when reporting the audit of the 2020/21 annual accounts and complete the checklist

Contact point for this section

61. The main contact point for this section of the Technical Bulletin is Neil Cameron, Manager (Professional Support) – ncameron@audit-scotland.gov.uk.

Section 3
Health sector

Auditing developments

Technical Guidance Note on risks of misstatement in 2020/21

62. Professional Support has published Module 13 of TGN 2021/1 to provide:

- guidance on applying the other modules to the audit of the annual report and accounts of health boards
- supplementary guidance on the risks of misstatements in the areas specific to health boards.

63. The TGN is available with supporting material to auditors on SharePoint* and is also freely available from the Audit Scotland website.

Auditor action
Auditors should pay due regard to TGN 2021/1

2020/21 model IARs

64. Professional Support has published TGN 2021/2(H) to provide auditors with the model IARs which should be used for the 2020/21 annual report and accounts. The TGN is available with supporting material to auditors on SharePoint* and is also freely available from the Audit Scotland website.

65. The model Independent Auditor's Reports set out in Appendices 1 and 2 of the TGN have been tailored to reflect health sector legislation and augmented by the reporting requirements of the Auditor General.

66. The changes are the same as for the central government sector set out at section 2.

Auditor action
Auditors should use this TGN when reporting the audit of the 2020/21 annual accounts and complete the checklist

Review of central work on CNORIS

67. Professional Support will be undertaking a review of the work carried out by the NHS Central Legal Office (CLO) relating to the Clinical negligence and other risks indemnity scheme (CNORIS). The objective of the review is to establish the extent to which the information prepared using the work of the CLO, as a management expert under ISA (UK) 500 can be used as audit evidence.

68. Professional Support will also evaluate the appropriateness of the methodology adopted by the Scottish Government to establish the total national liability for CNORIS. The review will focus on the estimation of the liability as at 31 March 2021 with a view to assessing the reliability of the methodology used for 2020/21.

69. Professional Support will then provide auditors with the outcome of the reviews to:

- inform auditors' evaluation of the relevance and reliability of the information prepared by the CLO as audit evidence
- provide assurance on the methodology used in the preparation of the CNORIS figures as at 31 March 2021 which are provided to boards.

Annual report and accounts developments

Guidance on 2020/21 accounts

70. The Scottish Government has issued guidance on the process and timeframes for the 2020/21 annual report and accounts of health boards.

71. The Technical Accounting Group has agreed that boards should follow the 2019/20 Manual for the Annual Report and Accounts for NHS Boards and Capital Accounting Manual for preparing their 2020/21 annual report and accounts, rather than issue updated manuals.

Auditor action
Auditors should refer to the 2019/20 accounts manual when auditing the 2020/21 annual report and accounts

72. Boards are required to also follow the 2020/21 FReM. Annex A of the guidance provides a summary of relevant changes to the 2020/21 FReM, and other changes, and their impact on the accounts manual. The annex clarifies that:

- the flexibility to omit the performance analysis provided by the 2020/21 FReM Addendum applies to health boards
- the required disclosures on financial performance and payments to suppliers should be made in the performance overview if the performance analysis is omitted
- The Governance Statement should meet the requirements of both the FReM and the Scottish Public Finance Manual.

73. In addition, the guidance advises that the timetable for submitting the accounts has been extended to Tuesday 31 August 2021 for draft accounts and 30 September 2021 for audited accounts.

Summary of auditor actions in this section

Paragraphs	Auditor actions
60-61	Pay due regard to TGN 2021/1 when performing the audit of 2020/21 annual report and accounts
62-64	Use TGN 2021/2(H) when reporting the audit of the 2020/21 annual accounts and complete the checklist
68-71	Refer to the 2019/20 accounts manual when auditing the 2020/21 annual report and accounts

Contact point for this section

74. The main contact point for this section of the Technical Bulletin is Neil Cameron, Manager (Professional Support) – ncameron@audit-scotland.gov.uk.

Section 4
Professional matters

Auditing developments

Consultation on reviews of audit profession

75. The UK Government has issued a consultation paper that sets out a package of measures to take forward the recommendations made by the following independent reviews:

- Sir John Kingman's Independent Review of the Financial Reporting Council (FRC) - referred to in Technical Bulletin 2019/1 (paragraph 125).
- the Competition and Market Authority (CMA)'s Statutory Audit Services Market Study - referred to in Technical Bulletin 2019/2 (paragraph 145).
- Sir Donald Brydon's Independent Review of the Quality and Effectiveness of Audit - referred to in Technical Bulletin 2020/1 (paragraph 88).

76. Some of the key proposals related to each review that may have an impact on public audit or are of particular interest are summarised in the following tables. Comments on the proposals should be sent to audit.consultation@beis.gov.uk by 8 July 2021.

Kingman review of FRC

Review recommendation	Government proposal
The FRC should be replaced with a new independent regulator named the Audit, Reporting and Governance Authority (ARGA).	The Government will legislate to establish ARGA when Parliamentary time allows. Chapter 10 sets out the proposed objectives and governance arrangements for ARGA.
The Government should review the UK's definition of a Public Interest Entity (PIE).	Paragraph 1.3.17 sets out two options for expanding the PIE definition, both of which would include the largest private companies. Paragraph 1.3.29 seeks views on other types of entity that could be included in a new PIE definition, including third sector entities with a public benefit purpose.
The regulator should work towards a position where individual audit quality inspection reports, including gradings, are published in full upon completion of reviews (AQR reports). As an interim step, AQR reports should be published on an anonymised basis.	The Government intends to legislate to allow AQR reports on individual audits to be published by the regulator without the need for consent from the audit firm and the audited body. The regulator will be free to decide whether this is publication in full or in summary form. The Government will put in place safeguards to prohibit the publication of sensitive information about audited bodies (paragraph 9.2.8).
The regulator's corporate reporting review (CRR) process should be extended to cover the entire annual report.	The Government will legislate to bring the entire content of the annual report within the scope of the CRR including any voluntary elements (paragraph 4.2.6).

Brydon review into the quality and effectiveness of audit

Review recommendation	Government proposal
ARGA should be the supervisory body for a new profession of corporate auditing.	The Government believes that a new, distinct professional body for corporate auditors should be created. Paragraphs 9.6.11 to 6.9.16 consider the best way of establishing such a body.
The Companies Act should be amended to replace 'true and fair' with 'present fairly, in all material respects'.	The Government considers that developing a new user guide to audit (which the FRC has agreed to take forward) is likely to be more effective in improving user understanding than replacing 'true and fair' (para 6.6.5).
There should be a mandatory Internal Controls Statement consisting of a signed attestation by the CEO and CFO to the Board on the effectiveness of the company's internal controls over financial reporting.	Paragraphs 2.1.14 to 2.1.39 consider options for strengthening the UK's internal controls framework. This includes an expanded role for external auditors in providing assurance that companies' internal controls are effective. It would involve the auditor in undertaking additional work to be in a position to express a formal opinion on the directors' assessment An initial preferred option is set out at paragraph 2.1.41. Under that option, decisions about whether the internal control effectiveness statement should be subject to external audit would usually be a matter for the audit committee.
Directors should report on the actions they have taken to prevent and detect material fraud. Auditors should state explicitly • the work performed to conclude whether the directors' statement is appropriate • the steps they have taken to assess the effectiveness of the relevant controls and to detect any such fraud.	Para 6.4.2 advises that the Government proposes to legislate to require • directors of PIEs to report on the steps they have taken to prevent and detect material fraud • auditors of PIEs to report on the work they performed to conclude whether the proposed directors' statement is factually accurate. The Government will discuss with the FRC the changes needed to require auditors to report on the steps they took to detect any material fraud and assess the effectiveness of relevant controls
Alternative Performance Measures (APMs) and KPIs linked to remuneration should be subject to audit.	The Government does not propose to introduce any further audit requirement for APMs or KPIs. It would welcome views, however, as to the effectiveness of the existing audit requirement for part of the Remuneration Report and whether this could be improved to promote better disclosure of financial metrics (para 6.7.7).

CMA Audit Market Study

Review recommendation	Government proposal
Mandatory joint audit	The Government has identified significant barriers to implementing joint audits. Instead paragraph 8.1.12 sets out the Government's proposal for a managed shared audit requirement for UK-registered FTSE 350 companies. This would involve an audit firm appointed to lead the group audit, with group entities being required to appoint a challenger audit firm to conduct a meaningful proportion of the audits.
An operational split between the audit and non-audit practices of the biggest firms	The Government has set out proposals at paragraphs 8.2.5 to 8.2.13 which share many of the key elements of the CMA's recommendations.

Guide on the impact of COVID-19 on materiality

77. The Institute of Chartered Accountants in England and Wales has issued a guide on the impact of COVID-19 on determining materiality. The guide advises auditors to consider whether changes to organisations caused by COVID-19 impact on materiality determinations. It suggests that materiality may be set at a lower level than previously for some audits, which could increase the scope and extent of audit testing. It recommends that auditors consider:

- whether the benchmark remains appropriate
- what percentage to apply
- whether lower specific materiality for certain account balances, classes of transactions and disclosures is needed
- the impact on performance materiality.

78. Specific considerations are summarised in the following table:

Area	Questions	Matters to consider
Determining overall materiality	Has the underlying business remained the same Is the business a similar size to previous years?	Projects put on hold Significant restructuring Different delivery models Effect on supply chains Likelihood of assets being impaired New financial arrangements
	Have the users of the accounts changed, or has their focus changed? Which KPIs are users interested in?	Over-optimism in significant estimates Opportunity to conceal non-COVID issues
	What benchmark has previously been used and is it appropriate in the current circumstances? What alternative benchmarks might there be?	Volatility of benchmark and whether averaging techniques have been used Types of adjustments to benchmark appropriate in the circumstances
Performance materiality	Have the risks increased? Is there an increased risk of override of controls, fraud or error? Has the control environment changed?	Incentives for management bias and manipulation of the accounts New transaction streams Greater estimation uncertainty. Changes in the design and implementation of controls
Lower specific materiality	Have line items become more material? Are there areas where there are increased risks? What are the areas of focus of users of the accounts?	Balances, classes of transactions or disclosures qualitatively material

Area	Questions	Matters to consider
Evaluating misstatements	What are the implications for misstatements brought forward in opening balances? Are there misstatements that would be material because of their nature?	Concerns over how COVID-19 impact is presented or disclosed Unadjusted misstatements brought forward Broader ranges when evaluating estimates
Reassessing materiality	Why might auditors need to reassess materiality and what are the implications for the audit?	Actual amounts for benchmark significantly different to forecast Impact on benchmark of material audit adjustments
Group audits	Are there specific group audit implications?	Early planning of scope of group audit
Communication with those charged with governance	Has materiality changed? Will more audit work be required?	Communicate early in the audit process if materiality expected to change or a stricter approach to adjusting for misstatements Impact of more audit work on fees

Paper on using technology in audits

79. The Financial Reporting Council (FRC) has published a paper on the use of technological resources in audit. This is an umbrella term for technology that assists the auditor in performing risk assessment procedures, obtaining audit evidence, and managing the audit process. The paper sets out the views of stakeholders as well as planned future actions.

80. The main findings are summarised in the following table:

Area	View
Impact on audit quality	The use of technology could significantly improve audit quality, when deployed at the right time in the audit process and by those with the right training.
Current standards	The current assurance model and ISAs do not represent a significant impediment to the development and deployment of technology in audit.
Application material	Additional application material and guidance would be beneficial.
Training and skillsets	Training and skillset are primary concerns. The recruitment of staff with the right skillsets alongside the development of appropriate training for current staff are priorities.
Data access	There are significant challenges in accessing high-quality data in a reliable and consistent format, meaning that the application of technological resources to improve audit quality can be practically challenging to deploy, requiring substantial work on the data itself before analysis can be conducted.

Proposals to revise quality management standards

81. The FRC has issued proposals to revise standards on audit quality which involves replacing the existing ISQC 1 and adopting:

- International Standard on Quality Management (UK) 1 Quality Management For Firms That Perform Audits Or Reviews Of Financial Statements, Or Other Assurance Or Related Services Engagements
- ISQM (UK) 2 Engagement Quality Reviews.

82. The proposed effective date of the new and revised standards is 15 December 2022. Comments were required by 18 March.

83. The proposed standards introduce a new quality management approach that is focused on proactively identifying and responding to risks to quality. Unlike extant ISQC 1, the new approach requires a firm to customise the design, implementation and operation of its system of quality management based on the nature and circumstances of the firm and the engagements it performs. The new approach also requires the firm to transition from policies and procedures that address standalone elements to an integrated approach that reflects the system as a whole.

A new approach that focusses on risk to quality

84. ISQM (UK) 1 introduces a new approach to quality management at the firm level that emphasises the responsibility of firm leadership for proactively managing quality, while at the same time being scalable to deal with differences in the size of firms and nature of the services they provide. ISQM (UK) 1 requires the firm to design and implement a risk assessment process to:

- establish quality objectives
- identify and assess quality risks
- implement responses to address those quality risks.

85. ISQM (UK) 1 focuses on those review findings that indicate that deficiencies may exist. Where positive outcomes or opportunities are identified as part of this process, the firm is encouraged to evaluate and respond to them. A consultation question explores making that a requirement.

86. More detailed requirements and related application material for engagement quality reviews are located in ISQM (UK) 2. It addresses the appointment and eligibility of an engagement quality reviewer and their responsibilities relating to that review. The revisions include:

- extending the requirement for an engagement quality review to engagements in addition to audits of financial statements
- enhancing the eligibility criteria for an individual to be appointed as an engagement quality reviewer
- enhancing the requirements and application material regarding the engagement quality reviewer's responsibilities, including the nature, timing and extent of the engagement quality review procedures performed
- consideration of the effect of engagement quality reviews, and other forms of engagement reviews, on the appropriate exercise of professional scepticism by engagement teams.

87. The proposals also include revising ISA (UK) 220 Quality Control For An Audit Of Financial Statements to reflect recent revisions to the international version of the standard. ISA 220 has been significantly revised resulting in a clear delineation of the responsibilities of the engagement partner and engagement team in relation to managing and achieving quality at the engagement level. There is also increased focus on taking into account the nature and circumstances of the audit engagement in managing quality at the engagement level.

Government response to Redmond Review

88. The UK Government has issued a response to the report from Sir Tony Redmond into the local audit of local authorities in England referred to in Technical Bulletin 2020/3 (paragraph 39). The response to each of the main recommendations are summarised in the following table:

Recommendation	Response
The creation of a new regulatory body called the Office of Local Audit and Regulation responsible for the procurement, contract management, regulation, and oversight of local audit.	The UK Government is not persuaded that a new body is required. It will explore other options for addressing the problems highlighted in the review including considering whether an existing body could take on the responsibilities.
Revising the current audit fee structure to ensure adequate resources are deployed.	Regulations are to be amended to allow the body that appoints auditors greater flexibility to ensure the costs of additional audit work are met.

Recommendation	Response
Deadline for published audited annual accounts to be extended from 31 July to 30 September.	Regulations are to be amended to extend the deadline to 30 September for 2020/21 and 2021/22 audits. The government will then review whether there is a continued need for an extended deadline.
An annual audit report to be submitted to the first full council meeting (rather than audit committee) after 30 September.	The government strongly agrees that submission should be to the full council and will explore but will consider whether the 30 September milestone is most appropriate.
Councils should appoint at least one independent member, suitably qualified, to the audit committee.	New guidance is to be issued which addresses these recommendations.
The facility for the Chief Executive, Monitoring Officer and Chief Financial Officer to meet with the Key Audit Partner at least annually should be formalised.	

89. In addition to the audit recommendations, the UK Government agrees with the recommendation related to the preparation of an audited simplified statement of service information and costs to enable comparison with the annual budget and council tax set for the year. The intention is for standardised statements to be communicated to all taxpayers and service users in England from 2021/22. The UK Government will explore how this can be done, for example alongside council tax bills.

90. The UK Government also agrees that the annual accounts should be reviewed to determine whether there is scope to remove disclosures that may no longer be considered to be necessary. The earliest this can be done is from 2022/23.

Contact point for this section

91. The contact point for this section of the Technical Bulletin is Paul O'Brien, Senior Manager (Professional Support) - pobrien@audit-scotland.gov.uk.

Section 5

Fraud and irregularities

Auditor action

Auditors should consider whether weaknesses in internal control which facilitated each fraud may exist in their bodies and take the appropriate action

92. This chapter contains a summary of fraud cases and other irregularities facilitated by weaknesses in internal control at audited bodies that have recently been reported by auditors to Professional Support.

Theft

Theft of assets and cash

93. An employee misappropriated cash and other assets valued at £237,000 from a public body over a period of eight years.

Key features

The theft was possible due to inadequacies in the reconciliation of a manual card recording system and management oversight.

The theft was identified when a new process for recording the cash and other assets was introduced and the perpetrator was moved to a new department. A subsequent internal audit identified the cash and assets were missing.

Police Scotland were informed. The employee admitted the theft, was prosecuted and imprisoned for over 3 years.

Procedures have been reviewed and improvements made.

Third party funds

94. A clerical assistant misappropriated over £7,000 from the accounts of vulnerable social care clients.

Key features

The clerical assistant committed the fraud by forging the signature of another staff member. The fraud was identified when another member of staff examined records of client funds and identified an entry that they had apparently authorised but had no knowledge of.

When interviewed, the clerical assistant admitted forging the signature of a colleague. An internal audit identified the full extent of the fraud.

The fraud was possible due to weakness in record keeping and in the oversight by management and the Corporate Appointee. Improvements have been introduced in relation to reconciliation processes and reviews of client accounts.

The matter was reported to Police Scotland and disciplinary processes were instigated. The clerical assistant has repaid the full amount.

Expenditure

Invalid supplier

95. A third party defrauded over £46,000 from a council by purporting first to be a council officer and then a supplier to the council.

Key features

One of the council's suppliers received an email purporting to be from the council asking if there were any outstanding invoices. The supplier replied attaching an invoice. The council then received an email purporting to be from the supplier with the invoice attached asking for it to be paid to a new bank account. The bank records were amended, and the invoice paid.

The fraud was identified when the genuine supplier contacted the council looking for payment of the invoice.

The fraud was possible as:

- the accounts payable department did not confirm that the change of bank details had been verified by the contracting service
- the officer within the contracting service had not received training on how to verify new bank details
- Indications within the e-mail that it was not genuine were missed
- learning from a previous unsuccessful similar attempted fraud involving the same supplier had not been shared with staff.

The council is introducing robust verification processes for change of bank details.

Grant payment

96. A third party defrauded £10,000 from a council by making a false claim for a business grant.

Key features

The perpetrator claimed a business grant for premises they had previously occupied. The fraud was identified when the legitimate business proprietor applied for a grant.

The fraudulent payment was possible as the council failed to identify that:

- the name on the business grant application was not the name of the business on the business rates system
- the bank statement used in support of the application was for a personal bank account rather than a business bank account.

More stringent checks are now carried out on grant applications and grants are now only processed by experienced staff.

The council are recovering the funds from the perpetrator.

Payroll

97. Third parties defrauded over £19,000 from three public bodies by re-directing salary payments.

Key features

In all cases, the payroll team received emails purporting to be from genuine members of staff, advising of a change to be made to bank account details. The payroll records were amended, and salary payments were made.

The frauds were identified when employees contacted the payroll team to query why they had not been paid.

The fraud was possible as the procedures in place to check the validity of bank detail changes had not been followed.

Payroll staff have been reminded of the proper procedures, including verification procedures for changes to employee bank account details. The cases have been referred to Police Scotland for investigation.

Technical Bulletin 2021/1

If you require this publication in an alternative format and/or language, please contact us to discuss your needs: 0131 625 1500 or **info@audit-scotland.gov.uk**

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Technical Bulletin 2021/2

Technical developments and emerging risks from April to June 2021

AUDIT SCOTLAND

Prepared for appointed auditors and audited bodies in all sectors

23 June 2021

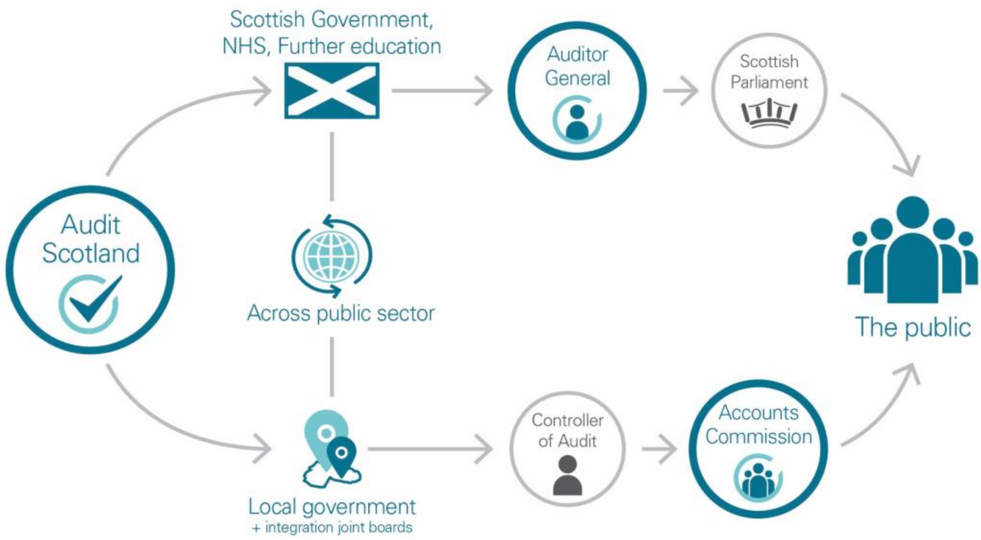
Who we are

The Auditor General, the Accounts Commission and Audit Scotland work together to deliver public audit in Scotland:

- The Auditor General is an independent crown appointment, made on the recommendation of the Scottish Parliament, to audit the Scottish Government, NHS and other bodies and report to Parliament on their financial health and performance.

- The Accounts Commission is an independent public body appointed by Scottish ministers to hold local government to account. The Controller of Audit is an independent post established by statute, with powers to report directly to the Commission on the audit of local government.

- Audit Scotland is governed by a board, consisting of the Auditor General, the chair of the Accounts Commission, a non-executive board chair, and two non-executive members appointed by the Scottish Commission for Public Audit, a commission of the Scottish Parliament.



About us

Our vision is to be a world-class audit organisation that improves the use of public money.

Through our work for the Auditor General and the Accounts Commission, we provide independent assurance to the people of Scotland that public money is spent properly and provides value. We aim to achieve this by:

- carrying out relevant and timely audits of the way the public sector manages and spends money

- reporting our findings and conclusions in public

- identifying risks, making clear and relevant recommendations.

Contents

Introduction

Purpose

Technical Bulletins provide information on developments and guidance on emerging risks

1. The purpose of Technical Bulletins from Audit Scotland's Professional Support is to provide auditors appointed by the Auditor General and Accounts Commission with:

- information on the main technical developments in each sector during the quarter
- information on professional matters during the quarter that are expected to have applicability to the public sector
- guidance on any emerging risks identified in the quarter.

2. Appointed auditors are required to pay due regard to Technical Bulletins. The information on technical developments is aimed at highlighting the key points that Professional Support considers auditors in the Scottish public sector require to be aware of. It may still be necessary for auditors to read the source material if greater detail is required. These can be accessed by using the hyperlinks. They are also available from the Technical Reference Library maintained by Professional Support.

3. The actions by auditors recommended by Professional Support in respect of each item are highlighted in red and are also summarised at the end of each section.

4. Technical Bulletins are also published on the Audit Scotland website and therefore are available to audited bodies and other stakeholders. However, hyperlinks in this bulletin indicated with an asterisk link to documents on the Technical Reference Library and therefore are active only for auditors.

Highlights summary

5. Professional Support draws attention in the following table to certain items in this Technical Bulletin:

Highlights summary		
Professional Support has published model Independent Auditor's Reports for local government [see paragraph 9]	Professional Support has published guidance on objections to 2020/21 local government annual accounts [see paragraph 14]	LASAAC has issued guidance on accounting for COVID-19 grants [see paragraph 17]
LASAAC has issued guidance on accounting for reserves [see paragraph 21]	CIPFA has issued guidance on the 2020/21 local government financial statements [see paragraph 35]	The Scottish Government has issued proposed revised statutory guidance on service concession arrangements [see paragraph 46]

Highlights summary		
The NAO has issued a disclosure guide for central government financial statements [see paragraph 59]	The Cabinet Office has issued guidance on the Remuneration and Staff Report [see paragraph 66]	Professional Support has issued an assurance report on CNORIS [see paragraph 73]
The Scottish Government has issued guidance on accounting by health boards for vaccines [see paragraph 75]	The Scottish Government has issued guidance on accounting by health boards for personal protective equipment [see paragraph 77]	The SFC has issued the 2020/21 accounts direction for colleges [see paragraph 88]
The SFC has issued the guidance on the 2020/21 accounts direction for colleges [see paragraph 90]	The FRC has issued a revised ISA (UK) 240 on fraud [see paragraph 94]	The UK Government has issued an updated response to the Redmond Review [see paragraph 96]

Contact point

6. The main contact point for this Technical Bulletin is Paul O'Brien, Senior Manager (Professional Support) – pobrien@audit-scotland.gov.uk.

Feedback on this Technical Bulletin is welcome

Section 1

All sectors

Auditor Action

Auditors should consider the application of this advice to their own audits

Advice to auditors

7. The following tables summarise requests for technical advice recently made by auditors to Professional Support in respect of the audit of the 2020/21 annual accounts which applies to all public bodies, along with the advice offered:

Property, plant and equipment

Can a valuer carry out a valuation if COVID-19 restrictions prevent the physical inspection of the property?
Where COVID-19 restrictions prevent a valuer from undertaking the physical inspection of a property, the Red Book allows a 'desktop' valuation to be performed using digital mapping, records, plans and other data. This involves the adoption of reasonable assumptions concerning relevant matters, such as the condition of the property. Dispensing with an inspection because of COVID-19 restrictions does not automatically lead to the need for a declaration of material uncertainty in relation to the valuation opinion. The decision on whether to make such a declaration rests with the valuer. The Red Book defines material uncertainty as where the degree of uncertainty in a valuation falls outside any parameters that might normally be expected. Consequently, less certainty and a higher degree of caution should be attached to the valuation than would normally be the case. For the avoidance of doubt, it does not mean that the valuation cannot be relied upon: Where no Material Valuation Uncertainty is declared, there are no specific disclosure requirements for the financial statements. However, bodies may judge it helpful to users if an explanation is provided in their accounting policy on revaluations. Where a Material Valuation Uncertainty is declared by the valuer, a clear explanation should be disclosed in the sources of estimation uncertainty note in the financial statements. Where properly disclosed and considered fundamental to understanding the accounts, auditors should include an Emphasis of Matter paragraph in the Independent Auditor's Report using the wording provided by Professional Support. In some circumstances, valuers may conclude that they are unable to form an opinion on the value from the information collected and provided. They would therefore be required to decline the instruction. Where that is the case, bodies should disclose an explanation in the financial statements. Regardless of any disclosures, auditors should consider qualifying their opinion on the financial statements on the basis of limitation of scope.

What indexation should public bodies use when valuing property in between formal valuations?
The Government Financial Reporting Manual (FReM) at paragraph 10.1.2 requires bodies to value their property using the most appropriate valuation process, and states that such processes might include a quinquennial valuation supplemented by either annual indexation or regular desktop valuation update. Indices are intended to reflect price movements anticipated over the course of the following financial year to provide indicative values at 31 March. The FReM does not specify a particular index but indicates that indices should be provided by a professional valuer. For health boards, paragraph 4.11.2 of the Capital Accounting Manual (CAM) expects the indices to be based on the Building Cost Information Service (BCIS) from RICS. The CAM is clear that indices are only appropriate for use on those properties measured at Depreciated Replacement Cost. In Professional Support's view, although the guidance in the CAM applies directly only to health boards, it is also useful for central government bodies. Indexation is rare in the local government sector but there is nothing to prevent it.

What indexation should public bodies use when valuing property in between formal valuations?

Auditors should evaluate whether:

- indexation is appropriate for the relevant asset, particularly where it is measured at fair value or existing use value
- the chosen index is reasonable
- information on the source of the index has been adequately disclosed.

Contact point for this section

8. The contact point for this section of the Technical Bulletin is Paul O'Brien, Senior Manager (Professional Support) - pobrien@audit-scotland.gov.uk.

Section 2
Local government sector

Auditing developments

2020/21 model Independent Auditor's Reports

9. Professional Support has published Technical Guidance Note (TGN) 2021/5(LG) to provide auditors with the model Independent Auditor's Reports (IARs) which should be used for the 2020/21 annual accounts. Auditors are required by the Code of Audit Practice to prepare their IARs in accordance with this TGN. The TGN is available with supporting material to auditors on SharePoint* and is also freely available from the Audit Scotland website.

10. The model IARs set out in Appendices 1 to 5 of the TGN have been tailored to reflect local government legislation and augmented by the reporting requirements of the Accounts Commission.

11. There are a number of changes to the model IARs as a result of revised versions of international standards on auditing (ISAs) applying in 2020/21 and other changes to the guidance. These are summarised in the following table:

Auditor action
Auditors should use this TGN when reporting the audit of the 2020/21 annual accounts and complete the checklist

Reason for change	Nature of change
Change to models arising from revised ISAs	• The assurance on the going concern basis of accounting is now in the form of a positive statement (rather than reported by exception). • The explanation of the extent to which the audit is considered capable of detecting irregularities has been revised to give greater focus to non-compliance with laws and regulations. • The opinions on the Remuneration Report and Statutory Other Information are now in separate parts of the model IARs, with the description of the auditor’s responsibilities for Statutory Other information clarified and moved to the latter part.
Changes in guidance	• Additional emphasis has been added of the requirement to discuss any modifications or additions to the model IAR with Professional Support, including any Emphasis of Matter paragraph. • Wording has been specified for use where auditors judge an Emphasis of Matter paragraph is appropriate where the declaration of a ‘material valuation uncertainty’ has been disclosed’.

12. The TGN also provides guidance on the amendments that require to, or may, be made to the wording in the models in the form of auditor actions. Auditors should complete for each report the checklist at Appendix 6 which provides a list of those auditor actions.

13. Any proposed modifications to any audit opinion or conclusion, or the inclusion of Emphasis of Matter or Other Matter paragraphs, should be discussed with Professional Support in advance of finalising the report.

Guidance on objections to 2020/21 annual accounts

14. Professional Support has published TGN 2021/3(LG) to provide auditors with guidance on the right of an interested person under section 101 of the Local Government (Scotland) Act 1973 to:

- inspect the unaudited 2020/21 annual accounts of a local government body
- object to those accounts.

15. The TGN is available with supporting material to auditors on SharePoint* and is also freely available from the Audit Scotland website.

16. Auditors should:

- evaluate whether the public inspection notice for 2020/21 is in accordance with applicable legislation
- carry out the actions set out in the TGN for any objections received.

Auditor action
Auditors should evaluate the 2020/21 inspection notice and deal with objections in accordance with this TGN

Financial statements developments

Guidance on COVID-19 grants

17. The Local Authority (Scotland) Accounts Advisory Committee (LASAAC) has issued guidance on the accounting and disclosure in 2020/21 for COVID-19 grants from the Scottish Government. The main consideration for local government bodies is to assess whether they are acting as the principal (i.e. the body is acting on its own behalf) or as an agent of the Scottish Government in the disbursement of the grants to third parties.

Local authorities need to assess whether they are principal or agent

18. A list of the various funding streams is provided at Appendix 1 of the guidance. This includes an initial assessment by a sub-group of LASAAC of the appropriate accounting treatment for each stream. The assessment indicates that bodies are acting as the principal for most funding streams, other than grants to support businesses and the £500 payment to social care staff. However, bodies are responsible for making their own assessments.

19. Where a body is acting as an agent, the transactions should not be recognised as income or expenditure in the Comprehensive Income and Expenditure Statement (CIES). It may be necessary to recognise a creditor or debtor in the Balance Sheet at the year end and the net cash position will be included in financing activities in the Cash Flow Statement.

20. There are no specific disclosure requirements relating to agent transactions. However, the guidance:

- expects inclusion of appropriate narrative explaining the body's role in distributing COVID-19 grants in the Management Commentary. This could include the total value of agency grants
- advises bodies to consider also disclosing the total amount of COVID-19 agency grants in a note to the financial statements. Inclusion in a note means that disclosure would be covered by the audit opinion on the financial statements.

Disclosure of information in Management Commentary and notes

Updated guidance on reserves

21. LASAAC has issued updated guidance on accounting for and disclosing reserves. The guidance represents proper accounting practices and, where it goes further than the accounting code or legislation, it represents mandatory guidance for Scottish local government bodies.

22. The guidance distinguishes between:

- usable reserves (i.e. those representing resources which the body can use to support service delivery)

- unusable reserves (as a result of statutory adjustments or accounting gains or losses recognised in other comprehensive income and expenditure).

Statutory power required for reserves

23. Scottish local government bodies can only create a usable reserve for external financial reporting purposes if they have a specific statutory power to do so. Applicable powers are set out at paragraph 15 of the guidance but are summarised in the following table:

Fund	Statutory power	Applicable bodies
General Fund	Section 93 of the Local Government (Scotland) Act 1973 (the 1973 Act)	All councils and bodies covered by section 106 of the 1973 Act
Capital Fund, Renewal and Repair Fund and Insurance Fund	Schedule 3 of the Local Government (Scotland) Act 1975	Councils, Regional Transport Partnerships and joint boards with the power to borrow
Capital Grants (and Receipts) Unapplied Account	Various statutory guidance	All councils and section 106 bodies

24. The guidance explains that:

No direct reserve accounting

- income cannot be credited directly to a reserve. It must first be recognised as income in the CIES, and then either remain in the General Fund or be transferred to one of the other statutory funds.

- expenditure cannot be debited directly to a reserve. It must first be recognised as an expense in the CIES, and then an equivalent amount is transferred to the General Fund from one of the other statutory funds.

- where a statutory fund is used to fund capital expenditure, an amount equivalent to the expenditure incurred should be transferred (debit) from that fund to the Capital Adjustment Account (credit).

Only historical cost depreciation is a statutory adjustment

25. Paragraph 50 of the guidance refers to the statutory adjustment made to the Capital Adjustment Account in respect of depreciation. The accounting code allows local government bodies to either:

- treat all depreciation as a statutory adjustment; or

- split depreciation into the historical cost element (statutory adjustment) and the valuation element (reserve transfer to Revaluation Reserve).

26. The guidance makes the second option mandatory. The option of treating the valuation element of depreciation as a statutory adjustment is therefore withdrawn from 2020/21.

27. Paragraph 19 explains that Scottish local government bodies can earmark part of the General Fund balance, but earmarked parts remain part of the General Fund and should not be described or presented as separate reserves (with the exception of the HRA balance). Paragraph 20 recommends that bodies draw a distinction between:

- ‘mandatory earmarked balances’, for example gains on financial instruments classified as fair value through profit or loss

- ‘voluntary earmarked balances’ reflecting the body’s discretionary financial management plans for the use of funds.

28. Paragraph 54 refers to a requirement in the accounting code that an analysis of earmarked reserves should be disclosed in a note. This guidance applies that requirement in Scotland and requires earmarked elements of the General Fund (or other statutory fund) to be disclosed in a note. An illustration of a disclosure note for the earmarked parts of the General Fund balance is provided at Appendix 1 of the guidance.

Earmarked elements should be disclosed in a note

29. Where deferred capital receipts (e.g. sales proceeds in instalments or a finance lease receipt) are held in a Capital Fund, paragraph 30 requires the relevant balance to be disclosed.

2019/20 report on actuarial information

30. Professional Support has arranged for PWC to provide a report* to support auditors when assessing the competence and objectivity of, and assumptions and approach adopted by, actuaries producing information required by IAS 19 figures in respect of the Local Government Pension scheme (LGPS) as at 31 March 2021. Auditors should refer to paragraphs 19 to 31 in Module 4 of Technical Guidance Note 2020/8(LG) for guidance on using the report and further information.

31. PWC have confirmed the competence and objectivity of the actuaries involved in valuations for the LGPS in Scotland. They are also comfortable that in aggregate the assumptions adopted by all actuaries will lead to liabilities falling within their expected ranges for all employers at 31 March 2021.

Actuarial assumptions are reasonable in typical cases

32. However, the report advises auditors to consider whether:

- local issues have been adequately covered in instructions issued by employers to actuaries (page 3)
- to subject the source data provided to the actuaries by employers to further audit procedures as discussed in section 4 of the report
- to establish actual asset returns and compare them with expected returns arrived at using market indices (see page 16)
- additional procedures are required for higher experience items on both the asset and liability side as a result of the funding valuations performed at 31 March 2020 (see page 17)
- material significant events have been communicated to the actuary and undertake additional audit procedures as appropriate (page 3).

Points for auditors to consider

33. Page 18 of the report provides a summary of the approach each actuary is taking for the McCloud judgement and the Goodwin case. In summary:

- All actuaries confirmed that for most employers an allowance for McCloud was made in the 2019/20 accounts. Any update (e.g. updated membership data due to the valuations at 31 March 2020) would therefore be recognised within Other Comprehensive Income (OCI).
- The majority of actuaries have confirmed that the 2020/21 service cost would include an allowance for the impact of McCloud (as one further year of service would need to be compensated for affected members).
- Appendix E summarises the approach to calculating the allowance taken by each actuary.
- Actuaries do not intend to make any specific allowance for the Goodwin case, unless requested to do so.

34. Page 22 of the report provides a summary of the approach being taken to Guaranteed Minimum Pension (GMP) indexation and equalisation:

- All actuaries have confirmed that they will make an allowance for full indexation for all members reaching statutory pension age from 6 April 2016, calculated using individual member data as at 31 March 2020.
- Most pension funds allowed for full indexation in 2019/20 and so any updates will go through OCI.
- None of the actuaries have made any allowance for any additional liabilities relating to GMP equalisation in view of the Treasury announcement that there was no impact on public service schemes.

Guidance on closing 2019/20 financial statements

35. The Chartered Institute of Public Finance And Accountacy (CIPFA) has issued Bulletin 9 Closure of the 2020/21 Financial Statements which provides guidance on the following areas of the 2020/21 financial statements that are relevant to Scottish bodies:

- Financial reporting issues arising from COVID 19
- Issued accounting standards not yet adopted
- Going concern basis of accounting
- Financial flexibilities.

Financial reporting issues arising from COVID 19

36. Paragraph 2 of the bulletin lists a range of potential financial reporting impacts of COVID-19, including on:

- property, plant and equipment, particularly where market value measurement is used
- financial instruments and investment property measured at fair value
- expected credit losses in financial assets
- reporting judgements and estimation uncertainty
- measurement of a local authority’s interests in other entities
- potential volatility in measurement of pension fund assets and liabilities.

37. Paragraph 39 advises that the Management Commentary should include a section on the local authority’s overall response to the pandemic including the administration of the various grants and reliefs administered on behalf of central government. This would include agent transactions to give a fuller picture of activity.

The Management Commentary should reflect the authority’s overall response to the pandemic

38. Paragraphs 49 to 51 provide guidance on COVID-19-related rent concessions such as a temporary rent reduction or rent holiday. It recommends that affected local authorities should follow the accounting treatment set out in the amendments to FRS 102 on this subject. These require a lessee to recognise any change in lease payments arising from rent concessions over the periods that the change is intended to compensate. This applies if, and only if, all of the following conditions are met:

- The change is a reduction in lease payments.
- Any reduction in lease payments affects only those payments originally due before applying the concession.
- There is no significant change to other terms and conditions of the lease.

Issued accounting standards not yet adopted

39. Paragraph 73 of the bulletin advises that the standards introduced by the 2021/22 accounting code that should be considered for disclosures in the 2020/21 financial statements as 'standards issued but not yet adopted' are:

- Definition of a Business: Amendments to IFRS 3 Business Combinations
- Interest Rate Benchmark Reform: Amendments to IFRS 9, IAS 39 and IFRS 7
- Interest Rate Benchmark Reform – Phase 2: Amendments to IFRS 9, IAS 39, IFRS 7, IFRS 4 and IFRS 16.

40. IFRS 16 Leases and IFRS 17 Insurance Contracts are excluded from these requirements as they have not been adopted by the 2021/22 accounting code.

Going concern basis of accounting

41. Paragraphs 81 to 83 of the bulletin highlight that the accounting code's requirement to use the going concern basis of accounting means that local government bodies cannot apply paragraph 25 of IAS 1 in respect of making an assessment of the body's ability to continue as a going concern.

42. This requirement applies regardless of the impact of COVID-19 on local authority financial sustainability because the rationale for requiring the going concern basis remains unchanged.

43. However, this is separate from the need for local government bodies to report on the impact of the COVID-19 in:

- the financial pressures in the Management Commentary
- the relevant liquidity reporting requirements under 7 Financial Instruments: Disclosures.
- credit risk disclosures.

Going concern basis of accounting remains appropriate but financial sustainability issues to be reported

Financial flexibilities

44. Paragraph 91 advises that the financial flexibilities allowed by the Scottish Government in respect of the use of capital receipts and deferring loans fund repayments (explained in Technical Bulletin 2021/1 – paragraphs 17 and 21) do not require changes to the accounting code.

45. If a local authority takes up the flexibilities available for 2020/21, it should consider the adequacy of any disclosures in relation to accounting policies and disclosure notes.

Proposed changes to statutory guidance on service concession arrangements

46. The Scottish Government has issued draft revised statutory guidance* on accounting for service concession arrangements. The revised statutory arrangements are being offered by the Scottish Government as a partial reform of the statutory arrangements as well as providing some financial flexibility to fund the impact of COVID-19.

47. The proposed guidance is permissive and there is no requirement to adopt any of the revised statutory arrangements, i.e. a local authority may continue to apply the current requirements set out in Finance Circular 4/2010. The guidance assumes a local authority will adopt one of the revised arrangements only when a financial benefit arises.

48. It is proposed that the revised statutory guidance will apply from 2020/21 but will have retrospective application. The options for proposed revised arrangement are:

- Restate to accounting standards. This is an irrevocable option to restate selected service concession arrangements onto an accounting standards basis in 2020/21 or a future year, with limited statutory adjustments for some impairments
- Reduce liability over asset life. Under this option, the liability repayment is charged over the useful life of the asset rather than the contract period. This may be applied to existing service concession arrangements where a local authority does not have the accounting records necessary to apply the accounting standards option, or has funded prepaid capital contributions and does not wish to revisit that
- COVID-19 flexibility. This is a short term option in response to the financial impact of COVID-19, and may only be implemented in either 2020/21 or 2021/22.

Three proposed new options

49. The proposed statutory adjustments related to each option, compared with the statutory adjustments required by Finance Circular 4/2010, are summarised in the following table:

Circular 4/2010	Restate to accounting standard	Reduce liability over asset life	COVID-19 flexibility
Statutory adjustment requiring prepaid capital contributions to be funded at 1 April 2009	Reversed	Not reversed	Not reversed
Statutory adjustment to exclude depreciation and impairment costs from the movement on the General Fund	Depreciation and impairment *within* the local authority's control charged to General Fund	Statutory adjustment to exclude depreciation and impairment costs from the movement on the General Fund	Statutory adjustment to exclude depreciation and impairment costs from the movement on the General Fund
Statutory charge to the General Fund equal to the unitary payment less service costs and finance costs charged to income and expenditure account *over the contract period*	Statutory adjustment reversed but new statutory adjustment for impairments *outwith* a local authority's control Also new statutory adjustment for any asset not depreciated	Statutory adjustment reversed but replaced with recalculated statutory adjustment charged in equal instalments *over asset life* (difference on recalculation credited to General Fund as a statutory adjustment)	Statutory adjustment reversed but replaced with recalculated statutory adjustment charged on *an annuity basis* (difference on recalculation credited to General Fund limited to any amount necessary to meet COVID-19 costs as a statutory adjustment)
Capitalised lifecycle replacement costs required to be charged to the General Fund as a statutory adjustment when the capital expenditure is incurred	Reversed	Not reversed	Not reversed

50. A working group has been set up comprising representatives from the CIPFA Directors of Finance Section, CoSLA, the Scottish Government and Audit Scotland to discuss the proposals and their potential wider implications.

Grant claims and returns

Non-domestic rates returns

2020/21 return and guidance

51. The Scottish Government has issued the 2020/21 Non-domestic rates notified return and guidance*. The most significant changes for 2020/21 are summarised in the following table:

Line	Relief	Change
2(a) and 2(b)	Intermediate property rate	A new rate has been introduced for property with rateable values between £51,000 and £95,000. The gross additional income compared with the basic property rate is included in line 2a and the net additional income is included in line 2b.
3(a) and 3(b)	Higher property rate	A new rate has been introduced for property with rateable values over £95,000. The gross additional income compared with the basic property rate is included in line 3a and the net additional income is included in line 3b.
25	Reverse vending machine relief	A new relief for equipment which recycles used beverage containers.
27	General relief	A new general 1.6% relief for all properties.
28	Retail, hospitality, leisure and airport relief	A new relief for certain properties in the retail, hospitality and leisure sectors, airports and certain properties situated at airports.

Guidance for auditors

52. Professional Support has published TGN/NDR/21 on certifying the 2020/21 non-domestic rates return. The TGN is provided with supporting material to auditors on SharePoint* and also on the Audit Scotland website.

Auditor action
Auditors should certify 2020/21 NDR returns using TGN/NDR/21

Housing benefit subsidy

53. Professional Support has published TGN/HBS/21 on certifying the 2020/21 housing benefit (HB) subsidy claim. The TGN is provided with supporting material to auditors on SharePoint* and also on the Audit Scotland website.

Auditor action
Auditors should certify 2020/21 subsidy claims using TGN/HBS/21

54. The Department for Work and Pensions (DWP) has issued the following modules of the Housing Benefit Assurance Process (HBAP):

- Module 3* comprising workbooks to be completed for detailed testing
- Module 5*, which is the software diagnostic tool along with the relevant checklist for Northgate Orbis systems.

55. The DWP has also issued LA Welfare Direct bulletin 5/2021 on the certification of 2020/21 claims. The bulletin:

- clarifies that auditors that have indirect access to DWP information on local authority systems or files must have gone through security checks. In Scotland, this is covered by the Disclosure Scotland checks undertaken on auditors.
- clarifies that local authorities are required to retain evidence such as claim forms, tenancy agreements etc to support the reperformance of benefit calculations required as part of the subsidy certification process

- reminded auditors that they are required to highlight cases in their letters to the DWP (and carry out associated error classification and extrapolations) where insufficient evidence has been retained by a local authority to support a claim.

56. In addition, the DWP has extended the submission deadline for the 2020/21 HB subsidy certification from 30 November 2021 (set out in TGN/HBS/21) to 31 January 2022, with a similar extension for 2021/22. However, the DWP has asked that local authorities and auditors work to the 30 November deadlines where it is practical to do so.

57. Where a subsidy claim will not be certified by the extended deadlines, the local authority is required to notify the DWP providing reasons for the delay. The normal subsidy withholdings will apply to all local authorities not meeting the extended deadlines.

Summary of auditor actions in this section

Paragraphs	Auditor actions
9 to 13	Use TGN 2021/5(LG) when reporting the audit of the 2020/21 annual accounts and complete the checklist
14 to 16	Evaluate the 2020/21 inspection notice and deal with objections in accordance with TGN 2021/3(LG)
52	Certify 2020/21 non-domestic rate returns using TGN/NDR/21
53	Certify 2020/21 subsidy claims using TGN/NDR/21

Contact point for this section

58. The contact point for this section of the Technical Bulletin is Paul O'Brien, Senior Manager (Professional Support) - pobrien@audit-scotland.gov.uk.

Section 3

Central government sector

Disclosure guide for 2020/21 financial statements

59. The National Audit Office has issued a disclosure guide on the 2020/21 financial Statements for bodies covered by the FReM.

60. The checklist is designed to ensure that bodies have prepared their 2020/21 financial statements in the appropriate form and have complied with all disclosure requirements. The guide is cross-referenced to the 2020/21 FReM, individual financial reporting standards, and the Companies Act 2006. A tailored checklist can be generated by selecting the criteria that are material to the body.

61. While the guide is designed primarily for the NAO's internal use, auditors in Scotland may also find it helpful. When checking that the FReM's disclosure requirements have been met, auditors should in accordance with the Overview Module of Technical Guidance Note (TGN) 2021/1:

- consider requesting that the body completes the disclosure checklist
- investigate the reasons for any non-compliance that the guide highlights
- evaluate whether the body's responses in the checklist are consistent with auditor's knowledge.

Auditor action
Auditors should consider using this disclosure guide

Guidance on accounting for grant payments

62. HM Treasury has issued application guidance on the accounting for grant payments from the perspective of the public body making the payment. The guidance specifically considers the application of IAS 37 to grantor accounting.

63. The guidance focuses on whether a body making a public statement about future intentions to award grants is an obligating event. Bodies need to judge whether an obligation has been created by the event which cannot be reneged upon. This would be the case if the body had no realistic alternative to settling that obligation. Whether it is an obligating event is dependent on:

- the nature of the announcement
- the details provided
- whether the body has undertaken any further actions or administrative processes that do create a valid expectation by those affected.

64. A body may or may not attach performance conditions to the payment of the grant. Examples of the considerations in each case are summarised in the flowing table:

Performance conditions	Considerations
No	When a public statement is made regarding offers of unilateral support, bodies need to consider whether it is communicated in a sufficiently specific manner to raise a valid expectation that the body will make the payment. Consideration needs to be given to the effect that eligibility criteria has on the timing of the recognition of a liability. Where eligibility could arise before the year end, consideration also needs to be given to the point at which the recipient could have a valid expectation of entitlement to the grant. Where a grant scheme requires a bid for funding, and the body has the discretion to reject the applications, the application process affects entitlement and therefore a valid expectation is not created the point of making the statement.
Yes	Liabilities may need to be recognised to the extent that the performance conditions have been fulfilled by the recipient. If the recipient has not fulfilled performance obligations, there is obligation at the year end.

65. If it has been determined that a constructive obligation exists, instances of a body not being able to reliably estimate the value of the liability are expected to be extremely rare.

Guidance on 2020/21 remuneration report

66. The Cabinet Office has issued Employer Pension Notice 626 on the preparation of the pay, pension and compensation disclosures for the Remuneration and Staff Report for 2020/21.

67. An example of the disclosures is provided at Annex 13C. There are no significant changes from 2019/20.

68. This guidance does not reflect the application of the FReM's requirements to Scottish bodies and therefore auditors should refer to Module 10 of TGN 2021/1.

Amendments to SPFM

69. The Scottish Government Finance Directorate has issued Finance Guidance Note 2021/1 which announces amendments to the Scottish Public Finance Manual (SPFM) in respect of:

- state subsidy
- internal control checklist.

70. The section on State Aid has been replaced by a new section named Subsidy Control to reflect that the EU State Aid regime was effectively revoked from UK law from 1 January 2021. The guidance applies to all public bodies who grant subsidies. Bodies are responsible for ensuring they understand the UK's commitments and comply with the obligations in relation to awarding subsidies.

71. The internal control checklist in the Certificates of Assurance section has been revised. New questions have been added on:

- processes to ensure bodies are able to assess their appetite to key risks
- fraud prevention measures to ensure they are built into plans when new grant schemes or other spend programmes are being developed

- the awareness of the role and responsibilities of an Information Asset Owner.

Summary of auditor actions in this section

Paragraphs	Auditor actions
59 - 61	Consider using the disclosure guide from the NAO

Contact point for this section

72. The contact point for this section of the Technical Bulletin is Neil Cameron, Manager (Professional Support) - ncameron@audit-scotland.gov.uk.

Section 4
Health sector

Auditing developments

Assurance report on 2020/21 clinical negligence claims

73. Professional Support has issued a report* to auditors following an examination of the Clinical Negligence and Other Risks Indemnity Scheme (CNORIS). The purpose of the report is to:

- provide assurance on the methodology used by the Scottish Government in the calculation of the CNORIS national obligation at 31 March 2021
- inform auditors' evaluation of the role of the NHS Central Legal Office as a management expert.

Auditor action
Auditors should refer to this report when auditing the 2020/21 provisions for CNORIS

Advice to auditors

74. The following table summarises a request for technical advice recently made by auditors to Professional Support in respect of the audit of the 2020/21 annual accounts which applies to all health bodies, along with the advice offered:

When will the Scottish Government issue revised guidance on the hospital services set aside?
The Scottish Government has advised Professional Support that they will not be issuing revised guidance on the hospital set aside for 2020/21. Previously agreed arrangements, allowing health boards and integration joint boards to agree a figure for the sum set aside based on the budget to be included in the financial statements remains in place, where partners are not able to fully comply with the guidance.

Financial statements developments

Guidance on vaccines and £500 payment to staff

75. The Scottish Government has issued guidance* on the treatment in 2020/21 of vaccines for COVID-19. The NHS Scotland Technical Accounting Group (TAG) considers that health boards are acting as agents of the Scottish Government throughout the vaccination process. Vaccines are therefore not to be accounted for as inventory by boards.

Health boards are acting as agents for the vaccine

76. The guidance also covers the £500 payment which the Scottish Government authorised boards to make, in accordance with PCS(COV)2020/1, to staff for working during the pandemic. TAG considered that a board is acting as:

- principal in relation to payments to their own staff (including employees, PFI employees and contractors)
- agents of the Scottish Government for payments to the employees of hospices.

Accounting for PPE and testing kits

77. The Scottish Government has issued guidance* on accounting for personal protective equipment (PPE) and testing kits. The guidance considers that a health board is acting as:

- principal in its use of PPE and testing kits for its own frontline staff

Health boards are acting as principal in the use of PPE and testing kits for its own staff

- agent in the provision of testing kits to the general public.

78. As the PPE and testing kits are provided to boards at no charge, accounting as principal entails recognising a non-cash grant at fair value and an equivalent amount of notional expenditure. NHS National Services Scotland (NSS) have provided boards with estimates of the costs of equipment provided. Boards should recognise these costs in their financial statements and disclose it in a separate line in note 3.

79. The Scottish Government is providing amended allocation letters to reflect the costs of equipment funded by Scottish Government. The cost of equipment supplied by the UK Government is not included in the allocation letter but should be recognised as a donation.

80. The auditor of NSS is reviewing the methodology used to arrive at the estimates provided to boards and will issue their conclusion to health board auditors.

GP sustainability loan scheme

81. The Scottish Government has issued guidance on the GP sustainability loan scheme*. All GP contractors who own their premises are eligible under the scheme to receive an interest-free secured loan from their health board of up to 20% of the existing-use value of their premises.

82. The loan should be recognised as a soft loan in the board's financial statements at the date the agreement is signed by both parties. The loan period should be assumed to be 20 years.

83. The letter provides further guidance on the subsequent accounting for the loan, including expected credit losses.

84. Loans will be repaid when the premises cease to be used for providing primary medical services under a contract with a health board or when they are sold, whichever comes first.

Statutory Other Information

Amendment to accounts manual

85. The Scottish Government has issued an update* to the accounts manual on the financial performance disclosure in 2020/21. The update reflects the pausing of the three-year financial planning process in 2020/21, and provides revised wording for disclosure in the Performance Report.

86. Although 2020/21 is not included in the three year break-even target, boards are nevertheless required to report on their annual performance for that year.

2020/21 is excluded from the 3 year planning requirement

Summary of auditor actions in this section

Paragraphs	Auditor actions
73	Refer to the Professional Support report on CNORIS when auditing the 2020/21 provisions for CNORIS

Contact point for this section

87. The contact point for this section of the Technical Bulletin is Neil Cameron, Manager (Professional Support) - ncameron@audit-scotland.gov.uk.

Section 5

College sector

2020/21 accounts direction

88. The Scottish Funding Council (SFC) has issued their Accounts Direction for Scotland's Colleges 2020/21. The direction requires colleges to:

- comply with the 2019 Statement of Recommended Practice: Accounting for Further and Higher education (SORP) in preparing their financial statements
- include a Performance Report and Accountability Report in their annual report and accounts in accordance with the FReM.

89. Specific mandatory disclosure requirements for colleges are set out in Appendix 2 to the direction. The main changes are as follows:

- Paragraph 9 has been added to clarify that the required disclosures in the Performance Report in respect of Cash Based Priorities and Adjusted Operating Position should be made in the performance overview section if a college elects to omit the performance analysis.
- Paragraph 28 has been added to clarify that colleges should comply with the FReM as well as the Scottish Public Finance Manual when preparing the Governance Statement

Governance statements should comply with the FReM and SPFM

Guidance on 2019/20 financial statements

90. The SFC has issued guidance notes on completion of the 2020/21 financial statements which are designed to supplement the accounts direction. The guidance covers key disclosures in the financial statements, including model disclosure notes set out at Annexes A to F.

91. There are no significant changes from 2019/20.

Contact point for this section

92. The main contact point for this section of the Technical Bulletin is Neil Cameron, Manager (Professional Support) – ncameron@audit-scotland.gov.uk.

Section 6
Professional matters

Auditing developments

Revised auditing standard on fraud

94. The Financial Reporting Council has issued a revised edition of ISA(UK)240 The Auditor's Responsibilities Related to Fraud in the Financial Statements. The revisions:

- are intended to address the recommendation in Sir Donald Brydon's review into the efficiency and quality of audits to clarify the obligations of auditors in respect of detecting fraud
- include enhancements of the requirements for the identification and assessment of risk of material misstatement due to fraud and the procedures to respond to those risks.

The revisions address the Brydon recommendation in respect of clarity over responsibilities

95. The revised standard is effective for audits of financial statements for periods commencing on or after 15 December 2021 (i.e. 2022/23 in the public sector), with early adoption permitted. The main revisions are summarised in the following tables:

Introduction

Paragraph	Proposal
3	Clarification that the evaluation of whether fraud is material should take into account the qualitative as well as quantitative characteristics of the fraud.
7-1	Clarification that the higher risk of not detecting a material misstatement resulting from fraud compared with error does not diminish the auditor's responsibility to obtain reasonable assurance about whether the financial statements are free of material misstatement due to fraud.

Professional scepticism

Paragraph	Proposal
12-1	New requirement that the auditor should not be biased towards obtaining evidence that may be corroborative or towards excluding audit evidence that may be contradictory.
13-1 and A9-1	Clarification that the auditor should remain alert for conditions that indicate a record or document may not be authentic. Examples are provided of conditions that may indicate a physical or electronic document is not authentic or has been tampered with.
14	New requirement for the auditor to investigate responses to inquiries that appear implausible.

Discussion among the audit team

Paragraph	Proposal
15-1 to 15-3 and A11	Specification of matters to be covered in the discussion, including how management could perpetrate and conceal fraudulent financial reporting and how assets of the entity could be misappropriated. Examples of matters that may be discussed are provided.
15-4 and A11-1	New requirement that the appointment lead should determine whether there should be further discussions at later stages in the audit to consider fraud risk factors. Examples of circumstances where it may be beneficial to have a further discussion are provided.

Risk assessments

Paragraph	Proposal
16	Clarification that the understanding obtained by the auditor includes the fraud risk factors relevant to the entity that affect the susceptibility of assertions to material misstatement due to fraud.
18-1	New requirement that the auditor makes inquiries of those persons who are responsible for dealing with allegations of fraud raised by employees or other parties.
21-1 and A20-1	New requirement for the auditor to discuss with those charged with governance the risks of material fraud in the entity, including those that are specific to the business sector.
21-2	Emphasis that the auditor should determine the implications for the audit if responses to inquiries of those charged with governance are inconsistent with the responses to the inquiries of management.
24-1, 33-1 and A48-1	New requirements that the auditor should determine whether the audit team requires specialised skills or knowledge to perform particular procedures and to investigate an identified fraud further for the purposes of the audit. Examples of matters that may affect the auditor’s determination are provided. There is supporting application material which includes identifying that the auditor may consider it appropriate to use a forensic accountant.

Responses to the assessed risks

Paragraph	Proposal
32-1	Emphasis that in evaluating possible management bias in making accounting estimates, the auditor should also comply with the relevant requirements in ISA (UK) 540.
36-1	Emphasis that in performing the overall evaluation of audit evidence, the auditor should evaluate whether: • the assessments of the risks of material misstatement at the assertion level due to fraud remain appropriate • sufficient appropriate audit evidence has been obtained regarding the assessed risks of material misstatement due to fraud, and should conclude whether the financial statements are materially misstated as a result of fraud.

Independent auditor’s report

Paragraph	Proposal
39-1	Clarification that, when explaining the extent to which the audit was considered capable of detecting irregularities, including fraud, the wording should not be 'boilerplate'.

Communications to management and those charged with governance

Paragraph	Proposal
42	New requirement that the auditor should consider any matters regarding management's process for identifying and responding to the risks of fraud and the auditor's assessment of the risks of material misstatement due to fraud.

Documentation

Paragraph	Proposal
45-1	Emphasis that the auditor should document how they addressed any identified information that is inconsistent with their final conclusion regarding a significant matter.

Updated government response to Redmond Review

96. The UK Government has issued an updated response to the report from Sir Tony Redmond into the local audit of local authorities in England.

97. In the original response (covered in Technical Bulletin 2021/1 – paragraph 88), the UK Government accepted the recommendation that there needed to be a single organisation with responsibility for leadership of the local audit system. This would include oversight of the quality framework and encouraging competition in the local audit market.

98. However, the government was not persuaded that a new body is required and indicated that it would explore other options including considering whether an existing body could take on the responsibilities. This update sets out the government's view that the system leader role should be undertaken by the new Audit, Reporting and Governance Authority (ARGA) which will replace the Financial Reporting Council. ARGA will have responsibility for local audit in respect of

ARGA to be the system leader for local audit in England

- producing annual reports summarising the state of local audit
- monitoring and review of local audit performance
- determining the code of local audit practice
- regulating the local audit sector.

99. The Public Sector Audit Appointments Ltd will continue to have responsibility for procurement and management of local audit contracts.

Contact point for this section

100. The contact point for this section of the Technical Bulletin is Paul O'Brien, Senior Manager (Professional Support) - pobrien@audit-scotland.gov.uk.

Section 7

Fraud and irregularities

Auditor action
Auditors should consider whether weaknesses in internal control exists in their bodies

101. This chapter contains a summary of fraud cases and other irregularities facilitated by weaknesses in internal control at audited bodies that have recently been reported by auditors to Professional Support.

102. Auditors should consider whether weaknesses in internal control which facilitated each fraud may exist in their bodies and take the appropriate action.

Misuse of assets

Misuse of a vehicle (1)

103. An employee of a public body defrauded almost £7,000 through unauthorised use of a car over a six-month period.

Key features

The employee continued to use a short-term hire car even after being provided with a leased car. Both cars were provided by the individual's employer.

The fraud was identified after the payroll team questioned why the car was still on hire.

The fraud was possible due to a lack of review and challenge by the line manager of the monthly car hire report for their department.

The officer was dismissed. The case has been reported to Police Scotland and options for civil recovery are being investigated.

Misuse of a vehicle (2)

104. An employee of a public body defrauded over £5,000 over an eight-month period through unauthorised use of a car.

Key features

The employee used a pool car for personal use after their own car broke down.

The fraud was identified after a finance report was issued to the budget holder suggesting that providing the employee with a small van would provide better value for money.

The fraud was possible as the budget holder failed to identify the pool car recharges and investigate accordingly.

Internal audit has reviewed the pool car system and identified areas for improvement.

Expenditure

Invalid supplier

105. A third party defrauded over £23,000 from a public body by purporting to be a supplier to the body.

Key features

A request was received by email to amend a supplier's bank account details. The supplier's email address had been intercepted by a fraudster who requested the change.

The fraud was possible as the public body did not telephone the supplier to verify the change of bank details.

The issue was identified when the genuine supplier queried why payment had not been received.

Internal audit has reviewed the change of bank details process. Improvements have been made to procedures and training has been provided for relevant staff.

The matter has been reported to the Police and Action Fraud UK has been notified of the case.

Income

Admission ticket income

106. Third parties defrauded over £8,600 in admission ticket income from a public body.

Key features

Unknown third parties fraudulently purchased admissions tickets for events using credit cards issued by an international provider. The loss was incurred where tickets had been used before the fraud was identified.

The fraud was discovered when the genuine cardholders subsequently requested refunds.

The fraud was facilitated by the international card provider not having secondary authentication procedures in place. The public body has stopped accepting credit cards without any secondary authorisation procedures in place.

Processes have been put in place to enhance card holder authentication for card payments.

Technical Bulletin 2021/2

April to June 2021

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Technical Bulletin 2021/3

Technical developments and emerging risks from July to September 2021

Prepared by Audit Scotland for appointed auditors and audited bodies in all sectors

20 September 2021

Contents

1. Introduction

Purpose

The purpose of Technical Bulletins from Audit Scotland's Professional Support is to provide auditors appointed by the Auditor General and Accounts Commission with:

- information on the main technical developments in each sector during the quarter
- information on professional matters during the quarter that are expected to have applicability to the public sector
- summaries of responses to requests for technical advice sought by auditors.

Appointed auditors are required by the Code of Audit Practice to pay due regard to Technical Bulletins. The information on technical developments is aimed at highlighting the key points that Professional Support considers auditors in the Scottish public sector require to be aware of. It may still be necessary for auditors to read the source material if greater detail is required. These can be accessed by using the hyperlinks. They are also available from the Technical Reference Library* maintained by Professional Support.

Any specific actions recommended by Professional Support to be taken by auditors are highlighted in green.

Technical Bulletins are also published on the Audit Scotland website and therefore are available to audited bodies and other stakeholders. However, hyperlinks in this bulletin indicated with an asterisk (*) link to documents on the Technical Reference Library and are only accessible by auditors.

Highlighted items

Professional Support highlights in the following table the items in this Technical Bulletin that may be of particular interest to auditors:

Highlighted items		
Professional Support has provided technical advice to auditors on emerging issues – paragraphs 1, 34 and 40	LASAAC has issued guidance on accounting for personal protective equipment provided free of charge – paragraph 2	The Scottish Government has issued draft statutory guidance on borrowing to fund a loan – paragraph 6

Highlighted items		
CIPFA/LASAAC has issued the accounting code for 2021/22 – paragraph 11	The Scottish Government has written to CoSLA on accounting for service concession arrangements – paragraph 16	CIPFA/LASAAC has issued the draft accounting code for 2022/23 – paragraph 20
Professional Support has published guidance on the risks of misstatements specific to colleges – paragraph 41	Professional Support has published model IARs for the college sector – paragraph 44	The FRC has issued new standards on audit quality management – paragraph 50
The FRC has issued a revised bulletin on auditor's reports in the private sector – paragraph 55	The FRC has issued guidance on data analytics – paragraph 59	The FRC has issued a statement on ESG challenges – paragraph 64

Contact point

The main contact point for this Technical Bulletin is Paul O'Brien, Senior Manager (Professional Support) – Pobrien@audit-scotland.gov.uk.

2. All sectors

Contact: Paul O'Brien, Pobrien@audit-scotland.gov.uk

Technical advice to auditors

Professional Support responds to requests for technical advice sought by auditors

1. The following tables summarise requests for technical advice recently sought by auditors from Professional Support in respect of the audit of the 2020/21 annual accounts which may apply to public bodies in all sectors, along with the advice offered:

The valuer declared a Material Valuation Uncertainty in the valuation report at 31 March 2020, which the body properly disclosed in the 2019/20 financial statements. The body has not arranged for a revaluation at 31 March 2021 but is continuing to make the same disclosure in the 2020/21 financial statements. Is that appropriate?
The body should discuss with the valuer any continuing impact of the prior year Material Valuation Uncertainty on values at 31 March 2021. Given the additional uncertainty over the values at 31 March 2020, it would be sensible for the body to have arranged for another valuation exercise at 31 March 2021. This applies regardless of whether a valuation would otherwise be due; the five-yearly interval between valuations is a maximum where circumstances allow and may not always be appropriate. Bodies have a responsibility to demonstrate that the carrying amount at 31 March 2021 materially reflects current value. If the body cannot provide sufficient reliable evidence, auditors should expect the body to arrange for a valuation at that date. The wording of the disclosure made in the 2019/20 financial statements is unlikely to be appropriate for 2020/21, and will need to be updated. If a valuation exercise is not necessary, the body should as a minimum discuss with the valuer whether the prior year Material Valuation Uncertainty still applied. It would be helpful to users of the financial statements if the body made a disclosure in the 2020/21 financial statements explaining that the prior year Material Valuation Uncertainty no longer applied. That is preferable to simply removing any reference and leaving the user to wonder what had happened. The disclosure should also provide justification for not arranging for an uptodate valuation.

The body uses a 1 April valuation date rather than 31 March. The exercise for the 1 April 2020 valuation date was carried out in the period January to May 2021 and the valuer has declared a Material Valuation Uncertainty. Is this appropriate?
There is nothing to prevent a 1 April valuation date, but it creates unnecessary problems. A valuation at 1 April 2020 is one year out of date by 31 March 2021 and, in effect, needs to be treated in the same way as a valuation at 31 March 2020, i.e. the body should allow for changes during 2020/21. For that reason, Professional Support's advice is to discourage a 1 April valuation date.

The body uses a 1 April valuation date rather than 31 March. The exercise for the 1 April 2020 valuation date was carried out in the period January to May 2021 and the valuer has declared a Material Valuation Uncertainty. Is this appropriate?

A valuation date of 1 April in 2020 is even more problematic than in other years. In effect, it artificially creates circumstances where a valuer may declare a Material Valuation Uncertainty, even though the work was carried out a year later. This additional complication strengthens the case for a valuation date of 31 March 2021. If the body declines to make that change, it will have to disclose the Material Valuation Uncertainty in the 2020/21 financial statements. However, it should disclose an explanation justifying that approach.

The body has changed valuer since the previous valuation 5 years ago. The property carrying amounts at 31 March 2021 have substantially increased in value compared with 31 March 2016, which is partially due to a change of valuation method. How should the increase in value be accounted for?

There are two main issues to consider here. First of all, a change in valuer does not necessarily lead to a change in the method adopted. It is for each body to determine the required approach and to instruct the valuer accordingly. It is important that bodies take responsibility for providing valuers with clear instructions. Auditors should:

- obtain the instructions and evaluate their clarity and appropriateness
- evaluate whether the body can demonstrate that the change in method is more appropriate and results in a more accurate estimate of property values. If the body cannot demonstrate this, the method should not be changed.

Aside from the change in method, if the increase in value is still substantial, unless there is evidence of a sudden increase in the last 12 months, it can reasonably be concluded that the increase in value has been accumulating evenly over the five years since the previous valuation. The increase may not have been material one year after the previous valuation, but the cumulative effect may have become material after say three years, and it should have been recognised in the carrying amount at that point. This would indicate that:

- the five year interval between formal valuations has been too long and should be reduced to three years going forward
- the carrying amounts at the end of years 3 and 4 (after the previous valuation exercise) were understated and an element of the increase should be treated as correcting a prior year error (i.e. by adjusting the value at 31 March 2020) rather than treating it all as an in-year increase.

A further consideration is whether a body revalues every asset in a class of property, plant and equipment simultaneously every five years or revalues a percentage of assets in that class every year. In Professional Support’s view, the latter approach is preferable as the movement in the value of those assets subject to the revaluation exercise can be used as a sense check of the carrying amounts of the remainder of the assets in that class.

3. Local government sector

Contact: Paul O'Brien, Pobrien@audit-scotland.gov.uk

Guidance on accounting for PPE supplied free

2. The Local Authority (Scotland) Accounts Advisory Committee (LASAAC) has issued an addendum to their guidance on accounting for coronavirus grants referred to in Technical Bulletin 2021/2 (paragraph 17). The addendum sets out the accounting treatment for personal protective equipment supplied free of charge to local authority social care staff by National Services Scotland (NSS) during 2020/21.

3. Where the equipment is used by local authority staff, the guidance considers that the authority is likely to be acting as a principal in the transaction. The authority should therefore account for the equipment at fair value in accordance with Code of Practice for Local Authority Accounting in the UK (accounting code). The accounting entries are set out at paragraph 11 of the addendum and are summarised in the following table:

Action	Account debited	Account credited
Stock recognition (paragraphs 5.1.2.8 and 5.1.2.9 of the accounting code)	Stock	Donated Inventories Account
Stock consumption (paragraph 5.1.2.18 of the accounting code).	Expenditure	Stock
	Donated Inventories Account	Income

4. Where the local authority passes on the equipment to third party providers, it is likely to be acting as an agent for the Scottish Government. The equipment is therefore not recognised by the authority.

5. The equipment flows through the IJBs which are acting as an agent regarding the transaction. However, IJBs need to consider whether these transactions need to be reflected in increased funding from partners and related increased commissioning expenditure. As the net financial impact of the equipment transactions on the partners is nil, the guidance advises that it would be reasonable to conclude that no impact on the IJB financial statements is required.

Consultation draft of statutory guidance on borrowing to lend

6. The Scottish Government has issued a consultation draft* of statutory guidance on the accounting treatment when a local authority has funded a loan from borrowing.

7. The consent of the Scottish Ministers is required where a local authority wishes to borrow to lend to a third party. Consent will only be given where the lending is to support capital expenditure of the third party. Where a local authority is given consent to borrow to lend to a third party, the authority is required to:

- make a loans fund advance at the point of making the external loan
- repay the loans fund advance over time as a charge to the General Fund each year
- recognise any repayment of the external loan as a capital receipt. This could be applied to fund the annual repayment of the loans fund advance (to neutralise the impact on the General Fund).

8. The proposal is to simplify the accounting by dealing with the loans fund repayment on a memorandum basis and for there to be no recognition (or application) of the capital receipt. There would therefore no longer be any impact on the General Fund.

9. However, charges will be required to the General Fund in the following circumstances:

- Any credit loss or other reduction in the debtor which is not matched with a repayment from the debtor would be a charge to the General Fund.
- A statutory charge to the General Fund will be required if the debtor does not repay a loan in the repayment period set by the Scottish Ministers. This will be equal to the outstanding loans fund advance. Any subsequent repayments will require the reversal of the statutory charge.
- If the debtor is written off, the outstanding amount would be a charge to the General Fund. In order to avoid the General Fund being charged twice for the same debtor, a reversal of the statutory charge would be necessary.

10. There is a similar proposal that loans fund repayments for loans to other statutory bodies or to common good funds should also be on a memorandum basis only.

2021/22 accounting code

11. The CIPFA/LASAAC Local Authority Code Board (CIPFA/LASAAC) has issued the accounting code* for 2021/22. The financial reporting framework is based on International Financial Reporting Standards (IFRS) and other pronouncements issued by the International Accounting Standards Board, adapted for the local government context where necessary. This is the first year that endorsement of IFRS is by the UK Endorsement Board rather than the EU.

12. The 2021/22 accounting code has been prepared on the basis of standards in effect for accounting periods commencing on or before 1 January 2021 (with the exception of IFRS 16 Leases).

13. The application of IFRS 16 has been deferred to 2022/23. Appendix F sets out the requirements agreed so far in respect of applying IFRS 16 in local government. Early adoption in 2021/22 is not permitted.

14. The changes in the 2021/22 accounting code are summarised in the Foreword. The changes are minor or simply provide clarification.

15. For example, paragraph 3.3.1.3 has been added to reflect that the accounting code adapts IAS 8 in respect of disclosing the impact of new accounting standards that have been issued but not yet adopted. The adaptation applies the disclosure requirement only to accounting standards that come into effect in the local government sector for financial years commencing on or before 1 January of the financial year in question (i.e. on or before 1 January 2022 for 2021/22). The addition is for clarification only as the requirement has been in effect for several years but was not previously explicitly described as an adaptation.

Proposed changes to statutory guidance on service concession arrangements

16. Technical Bulletin 2021/2 (paragraph 46) advised that the Scottish Government had issued draft revised statutory guidance on accounting for service concession arrangements. One proposal involved the short-term option to calculate the repayment of the service concession liability on an annuity basis in limited circumstances.

17. As a result of further discussions, the Scottish Government has written a letter* to COSLA to indicate that the statutory guidance will allow local authorities to repay a service concession arrangement liability on an annuity basis more generally. However, the authority will have to be able to demonstrate that it is both:

- prudent under the Prudential Code
- suitable, e.g. where the flow of benefits from an asset are expected to increase in later years, such as projects promoting regeneration or schemes where revenues will increase over time.

18. The decision to change to an annuity method of repayment must be taken by the full council. Any such change will be applied prospectively.

New flexibility to borrow to fund COVID-related costs

19. The Scottish Government has written a letter* to COSLA to advise of an additional financial flexibility that will enable local authorities to borrow to fund COVID-related revenue expenditure in 2021/22. A consent to borrow will be provided subject to the specified conditions being met, i.e. the local authority:

- could not balance its budget in 2020/21 and/or 2021/22
- must borrow from the Public Works Loan Board at a rate 1 percentage point higher than normal

- must undertake a review to identify any assets that could be sold to repay their borrowing; these assets must be sold in the next 3 to 5 years.

Consultation draft of 2022/23 accounting code

20. CIPFA/LASAAC has issued an invitation to comment (ITC) on the accounting code that will apply to 2022/23. The draft 2022/23 accounting code has been prepared on the basis of accounting standards and other pronouncements in effect for accounting periods commencing on or before 1 January 2022.

21. The main issues in the ITC are in respect of:

- the implementation of specific aspects of IFRS 16 Leases
- minor changes to accounting standards
- clarifying the disclosure requirement for the Capital Finance Requirement.

22. Responses should be sent to cipfalasaac@cipfa.org by 11 October 2021.

Implementation of IFRS 16 Leases

Measurement of service concession arrangement liability

23. Section 1A of the ITC proposes that service concession arrangement liabilities should be measured in accordance with the lease liability requirements of IFRS 16.

24. The principal difference from the current treatment based on IAS 17 is that where payments depend on an index or rate, IFRS 16 requires lessees to remeasure the liability to reflect changes to payments arising from changes in the index or rate.

25. The ITC also asks for any comments on the practical impact of adopting this approach, including whether there are any particular matters on which guidance would be helpful.

HRA tenancies

26. The accounting code includes an interpretation to the effect that all Housing Revenue Account (HRA) tenancies are deemed to be operating leases.

27. However, paragraph 37 of the ITC proposes an amendment to confirm that the practical expedient in the accounting code on transitioning to IFRS 16 (i.e. that a local authority should not reassess whether a contract is a lease at 1 April 2022) does not apply to HRA tenancies. This is necessary as HRA tenancies were not leases under IAS 17.

Changes to accounting standards

28. Sections B1 to B3 of the ITC set out proposals to reflect changes in accounting standards, some of which are summarised in the following table:

Standard	Nature of change	Proposed impact on accounting code
IAS 37 – onerous contracts	The amendment clarifies which costs should be included when assessing whether a contract will be loss-making. It specifies that the cost of fulfilling a contract comprises the costs that relate directly to the contract.	While amendments may affect specific cases prospectively, paragraph 38 proposes no substantive amendments to the accounting code.
IAS 16 - proceeds before intended use	The amendments prohibit an entity from deducting from the cost of property, plant and equipment (PPE) amounts received from selling items produced while the entity is preparing the PPE asset for its intended use. Instead, an entity recognises such sales proceeds and related cost in profit or loss.	Paragraph 40 expresses the view that this amendment in practice does not affect PPE under the accounting code, as it is measured at current value. No substantive amendments are therefore proposed.
IPSAS 42 Social Benefits	IPSAS 42 provides guidance on the recognition, measurement and disclosures of social benefits. These are defined as cash transfers paid to specific individuals and/or households to mitigate the effect of social risk and address the needs of society as a whole. IPSAS 42 recognises liabilities in the same way as IAS 37.	Social benefits are currently scoped out of section 8.2 of the accounting code. As IPSAS 42 recognises liabilities in the same way as IAS 37, paragraph 48 proposes removing that scope exclusion.

29. In addition, section D1 of the ITC refers to IFRS 17 Insurance Contracts which has a revised effective date of 1 January 2023. Subject to UK adoption, the earliest year for local government adoption would be 2023/24.

30. A working group has been established by HM Treasury to consider early implementation issues of IFRS 17. This includes considering the extent to which the public sector may have contracts meeting the relevant criteria.

31. Paragraph 64 requests further information on the applicability of IFRS 17. Appendix 2 sets out some areas where potential issues for local authorities may exist, and provides guidance on matters which respondents might consider when making their response. The areas include: pension guarantees; mutual insurance and other transactions explicitly framed as insurance; economic development support; cases where local authorities are providing insurance while acting as an intermediary; and cases where local authorities are providing warranties.

Disclosure requirement for the Capital Finance Requirement

32. The consultation process on the 2021/22 accounting code indicated that some local authorities were having difficulty determining the appropriate amount for the Capital Finance Requirement (CFR) which is required by the accounting code to be disclosed. The components of the CFR are specified at paragraph 79 of the Prudential Code and should be extracted from information in the local authority's Balance Sheet.

33. Paragraph 69 of the ITC proposes amending the wording in the accounting code so it is clear that:

- it is the actual (as opposed to estimated) CFR that should be disclosed
- the CFR amount should be as specified by the Prudential Code.

Technical advice to auditors

Professional Support responds to requests for technical advice sought by auditors

34. The following tables summarise requests for technical advice recently sought by auditors from Professional Support in respect of the audit of the 2020/21 annual accounts of local government bodies, along with the advice offered:

Can a local authority continue to treat the full depreciation charge as a statutory adjustment in 2020/21?
In previous years, the full depreciation charge was transferred as a statutory adjustment from the General Fund (credit) to the Capital Adjustment Account (debit). In addition, there was a reserve transfer from the Revaluation Reserve (debit) to the Capital Adjustment Account (credit) for the revalued element of deprecation (i.e the additional depreciation charged as a result of the asset being carried at current value rather than historical cost). Although this treatment continues to be permitted by the 2020/21 accounting code, it is no longer permitted for Scottish authorities as a result of mandatory guidance from LASAAC. The LASAAC guidance restricts the statutory adjustment to depreciation on the asset's historical cost. Depreciation on the asset's revalued element should be the subject of reserve transfer from the Revaluation Reserve (debit) to the General Fund (credit).

The council has not included resources transferred from the health board for community care or additional Social Fund contributions via the NHS for social care COVID-19 pressures in its disclosure note for grant income. Do these items constitute a grant or are they revenue from a customer?
The main consideration is whether the transaction is: • an exchange transaction, i.e., the council provides services to the health board of an approximately equal value in exchange for the income (which would indicate it is revenue from a customer under IFRS 15); or • a non-exchange transaction, i.e. the council does not provide the health board with approximately equal value in exchange (which would indicate a grant under IAS 20).

The council has not included resources transferred from the health board for community care or additional Social Fund contributions via the NHS for social care COVID-19 pressures in its disclosure note for grant income. Do these items constitute a grant or are they revenue from a customer?

In the case of social care funding that flows through health boards to local government, health boards are required by Scottish Government to pass this funding to the council. The health board does not gain anything in exchange for providing the funding. Such funding should be recognised and disclosed as grant income.

A similar argument applies to resource transfer funding provided by the health board to the council. As the health board does not receive any distinct good or service in return for provision of the funding, it is appropriate to treat it as a grant.

Grant claims and returns

Housing benefit subsidy

35. The Department for Work and Pensions has issued the Module 5 Software Diagnostic Tool* component of the HBAP approach to the certification of the 2020/21 housing benefit subsidy claims for councils using Capita, Civica and Northgate benefit systems.

Non-domestic rates

36. The Scottish Government has issued Finance Circular 8/2021 Business Rates Incentivisation Scheme 2019 - 22 to:

- provide details of the outcome of the Business Rates Incentivisation Scheme (BRIS) for 2019/20
- confirm that BRIS has been suspended for both 2020/21 and 2021/22.

37. Annex A sets out the sums to be retained under the BRIS for 2019/20. For 2020/21 and 2021/22, some Non-Domestic Rates Income has been converted to General Revenue Grant for the cost of COVID-19 reliefs.

4. Central government sector

Contact: Neil Cameron, Ncameron@audit-scotland.gov.uk

Revised guidance on severance and settlement agreements

38. The Scottish Government has issued Finance Guidance Note 2021/3 to advise of amendments to the Scottish Public Finance Manual chapter on severance and settlement agreements.

39. The main amendments to the chapter clarify that:

- the severance policy applies to all bodies except where it is inconsistent with any statutory requirements
- the maximum payback period of 24 months for voluntary severance applies in all cases except where a body's own compensation scheme has a shorter payback period
- the purpose of the £95,000 cap is to restrain settlement payments from going excessively beyond what a body is legally obliged to pay
- notice periods for voluntary severance are expected to be worked and outstanding leave taken prior to termination of employment.

Technical advice to auditors

Professional Support responds to requests for technical advice sought by auditors

40. The following table summarises a request for technical advice recently sought by auditors from Professional Support in respect of the audit of the 2020/21 annual accounts of central government bodies, along with the advice offered:

The central government body presents a Foreword and other statements in its annual report and accounts separate from the Performance Report and Accountability Report, and there is no cross-reference. How should these statements be reflected in the Independent Auditor's Report?
The Government Financial Reporting Manual (FReM) requires the annual report and accounts to comprise the following three elements: financial statements, Performance Report and Accountability Report. The expectation is that all information in the annual report and accounts should fit into one of those elements, and therefore the model Independent Auditor's Reports are designed on that basis. If a body positions a foreword or other statement outside that specified structure, it may impact on the opinions expressed on, and the description provided for, Statutory Other Information in the Independent Auditor's Report.

The central government body presents a Foreword and other statements in its annual report and accounts separate from the Performance Report and Accountability Report, and there is no cross-reference. How should these statements be reflected in the Independent Auditor's Report?

Auditors should request that the information contained in the separate foreword or other statement be brought within the Performance Report or Accountability Report. This can be done by either physically relocating the information or by simply adding a cross-reference to it. This is essential if the information is meeting a requirement of the FReM, but is recommended in any event. The outcomes are as follows:

- If the body accepts the request, no changes are required to the Independent Auditors Report.
- If the body declines to either relocate the information or even add a cross-reference, the relevant FReM requirement should be treated as not being met. Auditors should discuss with Professional Support a possible qualified opinion in respect of Statutory Other Information as a result of non-compliance with the FReM.
- If the information is not necessary to meet a requirement of the FReM, it does not impact on an opinion. However, auditors should consider whether it represents clutter and request it be removed from the annual report and accounts.

The model Independent Auditor's Reports describe Statutory Other Information as the Performance Report and the Accountability Report (except for the audited part of the Remuneration and Staff Report). Any foreword or any statement outside that specified structure (without a cross-reference) does not represent Statutory Other Information. It will be necessary to extend the wording of the description to encompass voluntary other information. Auditors should discuss with Professional Support the amendments required.

The same principle applies in local government for information outside the Management Commentary or Annual Governance Statement.

5. College sector

Contact: Neil Cameron, ncameron@audit-scotland.gov.uk

Technical Guidance Note on risks of misstatement in 2020/21

41. Professional Support has published Module 14 of Technical Guidance Note (TGN) TGN 2021/1. The TGN is intended to inform auditors' judgement when identifying and assessing the risks of material misstatement in the 2020/21 annual report and accounts of central government bodies generally. Module 14 provides:

- guidance on applying the other modules to the audit of the annual report and accounts of colleges
- supplementary guidance on the risks of misstatements in the areas specific to colleges.

42. The TGN supplements the Code of Audit Practice and auditors are expected to pay the TGN due regard and use it as a primary reference source when performing 2020/21 audits.

43. The TGN along with Module 14 is available with supporting material to auditors on SharePoint* and is also freely available from the Audit Scotland website.

Technical Guidance Note on 2020/21 model IARs

44. Professional Support has published TGN 2021/6(C) to provide auditors with the model Independent Auditor's Reports (IARs) which should be used for the 2020/21 annual report and accounts. The TGN is available with supporting material to auditors on SharePoint* and is also freely available from the Audit Scotland website.

45. The model IARs set out in Appendices 1 and 2 of the TGN have been tailored to reflect college sector legislation and augmented by the reporting requirements of the Auditor General.

46. There are a number of changes to the model IARs as a result of revised versions of international standards on auditing (ISAs) applying in 2020/21 and other changes to the guidance. These are summarised in the following table:

Reason for change	Nature of change
Change to models arising from revised ISAs	The assurance on the going concern basis of accounting is now in the form of a positive statement (rather than reported by exception).

Reason for change	Nature of change
	The explanation of the extent to which the audit is considered capable of detecting irregularities has been revised to give greater focus to non-compliance with laws and regulations. The opinions on the Remuneration and Staff Report and Statutory Other Information are now in separate parts of the model IARs, with the description of the auditor's responsibilities for Statutory Other information clarified and moved to the latter part.
Changes in guidance	Additional emphasis has been added of the requirement to discuss any modifications or additions to the model IAR with Professional Support, including any Emphasis of Matter paragraph. Wording has been specified for use where auditors judge an Emphasis of Matter paragraph is appropriate where the declaration of a 'material valuation uncertainty' has been disclosed'.

47. The TGN also provides guidance on the amendments that require to, or may, be made to the wording in the models in the form of auditor actions. Auditors should complete for each report the checklist at Appendix 3 which provides a list of those auditor actions.

48. Any proposed modifications to any audit opinion or conclusion, or the inclusion of Emphasis of Matter or Other Matter paragraphs, should be discussed with Professional Support in advance of finalising the report.

49. Auditors should use this TGN when reporting the audit of the 2020/21 annual report and accounts and complete the checklist.

6. Professional matters

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New audit quality management standards

50. The Financial Reporting Council (FRC has issued new standards on audit quality management in International Standards on Quality Management (ISQM) 1 and 2. These standards replace the extant standard that deals with a firm's responsibilities for its system of quality control (ISQC (UK) 1) for financial statement periods beginning on or after 22 December 2022.

51. The new standards introduce a quality management approach that is focused on proactively identifying and responding to risks to quality. Unlike extant ISQC (UK) 1, the new approach requires a firm (including public sector equivalents) to customise the design, implementation and operation of its system of quality management based on the nature and circumstances of the firm and the engagements it performs. The new approach also requires the firm to transition from policies and procedures that address standalone elements, as required by extant ISQC (UK) 1, to an integrated approach that reflects upon the system as a whole.

52. ISQM (UK) 1 introduces a new approach to quality management at the firm level that emphasises the responsibility of firm leadership for proactively managing quality, while at the same time being scalable to deal with differences in the size of firms and nature of the services they provide. The new standard requires the firm to design and implement a risk assessment process to:

- establish quality objectives
- identify and assess quality risks
- implement responses to address those quality risks.

53. ISQM (UK) 1 focuses on those review findings that indicate that deficiencies may exist. Where positive outcomes or opportunities are identified as part of this process, the firm is encouraged, but not required, to evaluate and respond to them.

54. ISQM (UK) 2 applies to all engagements for which an engagement quality review is required to be performed in accordance with ISQM (UK) 1. An engagement quality review is an objective evaluation of the significant judgments made by the audit team and the conclusions reached thereon, completed before the date of the auditor's report. An engagement quality reviewer may be a partner, other individual in the firm, or an external individual, appointed to perform the engagement quality review. ISQM(UK) 2 deals with the:

- appointment and eligibility of the engagement quality reviewer

- engagement quality reviewer's responsibilities relating to the performance and documentation of an engagement quality review.

Revised bulletin on auditor's reports in the private sector

55. The FRC has issued Bulletin - Illustrative Auditors Reports on Private Sector Financial Statements (August 2021). The auditor's reports set out in the Appendices to the bulletin illustrate:

- how the requirements of ISA (UK) 700 could be applied to private sector entities
- the requirements of the law and regulations applicable to the particular type of entity to which the illustration applies.

56. The reports are illustrative and other approaches may be adopted provided that the form and content of the auditor's report meets the requirements of ISA (UK) 700.

57. The bulletin has been updated to reflect legislative changes post the EU withdrawal transition period. It is applicable to financial statements for periods commencing after 1 February 2020 with filing after 31 December 2020.

58. Professional Support provides model auditor's report which are consistent with the illustrative examples contained in the bulletin but tailored to reflect Scottish public sector legislation and augmented by the reporting requirements of the Auditor General and the Accounts Commission.

New guidance on data analytics

59. The FRC has issued guidance on Addressing Exceptions in the use of Audit Data Analytics. For the purposes of the guidance, Audit Data Analytics (ADAs) are data analytic techniques that can be used to perform risk assessment, tests of controls, substantive procedures or concluding audit procedures.

60. The purpose of the guidance is to aid auditors in dealing with the large volume of outliers generated when using ADA. The guidance uses the following key terms:

- Outliers – means results generated by an ADA that do not match the auditor's initial expectation for the population.
- Exceptions – means the auditor has analysed the outliers and determined that they are truly exceptions and not generated as a result of inappropriate tool scoping, poorly defined initial parameters, or the use of poor-quality data.

61. A significant volume of outliers is a symptom of poorly defined parameters. Parameters may require re-calibration after initial analysis to ensure the tool is appropriately identifying outliers that merit further investigation as exceptions.

62. Page 4 of the guidance sets out some considerations for the auditor in determining whether the use of ADA is appropriate. For example, whether the data is of sufficient quality to support meaningful analysis, i.e. it is complete, accurate, valid, and accessible in a format which facilitates analysis.

63. The remainder of the guidance:

- sets out a general approach to addressing outliers generated when using ADA to test a single population (pages 5 and 6)
- covers refining the parameters of a tool after its initial application (page 7)
- provides an example of testing revenue (page 8).

Statement on ESG challenges

64. The FRC has issued a Statement of Intent on environmental, social and governance (ESG) challenges. The purpose of the statement is to set out the challenges to reporting on ESG issues in a way that meets the needs of stakeholders, some possible actions for addressing those challenges, and the FRC's planned activities in this area.

65. The FRC has grouped the challenges into six stages. Each stage along with the related challenges and examples of actions planned by the FRC are summarised in the following table:

Stage	Summary of challenges	Summary of FRC actions
Production – better internal information leads to better decisions and insight for stakeholders	Companies face challenges in how they measure, manage, control and assure ESG data. This situation is compounded by multiple thresholds, frameworks and guidance, as well as stakeholders having different information needs. Often reporting is aspirational and high level and does not provide users with information about progress, whether the entity's strategy will deliver the commitment, and whether financial statements are aligned with the commitment.	The FRC will: • ensure that the requirements for information are based on sound internal frameworks and methodologies, and that the system supports the standardisation and consistency of such methodologies • work with partners to improve the use of quality non-financial information • consider these issues within future revisions to the Guidance on the Strategic Report to strengthen the framework and deliver coherent and accessible information • develop guidance on the impact of climate-related issues on the financial statements, and consider whether changes need to be made to the accounting standards.

Stage	Summary of challenges	Summary of FRC actions
Audit and assurance – reported information is robust and reliable	The current level of data maturity is unlikely to be sufficient to enable a reasonable assurance opinion to be provided. However, a limited assurance opinion may be insufficient to meet expectations. Financial statements may not take proper account of material ESG issues.	The FRC will: • encourage the development of internal methodologies to ensure information is robust and aligns with the external reporting framework. • ensure that information is capable of being subject to assurance and provides high quality, consistent and comparable reporting • consider ESG-related amendments within future revisions of the auditing and assurance standards. • issue ESG-related audit and assurance guidance.
Distribution – information is made accessible to interested parties	ESG information is often located in separate places, reports and media at different dates and often not in an accessible or reusable format.	The FRC will: • ensure that there is an appropriate framework for information to be made publicly available on a more consistent basis • encourage the electronic distribution of ESG data and a digital tagging system.
Consumption – information leads to better decision making by stakeholders	Users have difficulty obtaining ESG data and it is often based on incomplete frameworks and differing methodologies, has limited comparability, or is not timely. The lack of useful and useable information results in stakeholders finding it difficult to make effective decisions.	The FRC will ensure that the reporting framework delivers information that is fair, balanced, and understandable, transparent, consistent, and comparable.
Supervision – information and activity is appropriately monitored and requirements are enforced	There is a need to supervise whether companies, auditors and assurance providers meet relevant existing and future requirements.	The FRC will: • assess the degree to which auditors ensure that companies take appropriate account of ESG issues in their annual report and accounts. • hold to account those who do not meet requirements.

Stage	Summary of challenges	Summary of FRC actions
Regulation – coordinated and coherent regulation leads to efficiency	There is a need to ensure that international ESG standards work effectively alongside a domestic framework. Greater coordination is needed to ensure there is an effective reporting ecosystem.	The FRC will: • develop a vision for what ESG reporting can deliver in the longer term, and how this can best be achieved • seek better regulatory coherence and the reduction of unnecessary overlap and confusion in requirements • support the movement towards global sustainability reporting standards • influence the development of IFRS where there are specific issues relating to ESG.

Feedback on future of corporate reporting discussion paper

66. The FRC has issued a Feedback Statement following their discussion paper on the future of corporate reporting (referred to in Technical Bulletin 2020/4 – paragraph 94).

67. The discussion paper set out a new, principles-based framework for corporate reporting. The central idea was a network of interconnected reports; with the full financial statements, a Business Report and a Public Interest Report at the core; and a series of network reports providing more tailored information across a range of topics.

68. Pages 5 to 15 of the statement set out the feedback provided by respondents. In summary, respondents were supportive of some aspects of the proposals. For example, they:

- broadly supported a reporting model that accommodates the information needs of investors and wider stakeholders; the development of guiding principles; the concept of the reporting network; and the development of standards for non-financial reporting

- supported the importance of firms providing information about how they view their obligations in respect of the public interest, although support was more muted for a standalone Public Interest Report

- strongly supported the role of technology and the importance of non-financial reporting in any future corporate reporting model.

69. However, respondents called for the FRC to consider the practical challenges of implementing the proposals, including the level of audit and assurance over the different reports within the network.

70. There were mixed views on whether an objective-driven model (that was neutral regarding the audience) should replace the current model where the content of the report is determined by reference to the information needs of the primary users. One of the challenges identified with the objective-driven approach was determining materiality.

Proposed auditing standard on less complex bodies

71. The International Auditing and Assurance Standards Board (IAASB) has issued an exposure draft of a proposed international standard on auditing the financial statements of less complex bodies.

72. The proposals recognise that the complexity in the ISAs poses challenges for audits of less complex entities. This stand-alone standard has been designed to be proportionate to the typical nature and circumstance of an audit of these entities.

73. Comments should be submitted via the IAASB website by 31 January 2022.

7. Fraud and irregularities

Contact: Anne Cairns, Acairns@audit-scotland.gov.uk

This chapter contains a summary of fraud cases and other irregularities facilitated by weaknesses in internal control at audited bodies that have recently been reported by auditors to Professional Support.

Auditors should consider whether weaknesses in internal control which facilitated each fraud may exist in their bodies and take the appropriate action.

Auditors should also refer to the annual Fraud and Irregularity Report.

Pension payments

74. A family member of a deceased pensioner continued to collect £300,000 of pension payments over a 21-year period from a public sector pension fund.

Key features
The pension fund was not notified of the death of the pensioner and the pension payments continued to be paid.
The fraud was discovered by the pension fund after mail sent to the deceased pensioner was returned.
The fraud was possible as the pensioner's death pre-dated data matching controls which are now in place to automatically highlight when a pensioner has died.
The pension payments have been stopped and the matter reported to Police Scotland.

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Technical Bulletin 2021/3

Technical developments and emerging risks from July to September 2021

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Technical Bulletin 2021/4

Technical developments and emerging risks from October to December 2021

AUDIT SCOTLAND

Prepared by Audit Scotland for appointed auditors and audited bodies in all sectors

14 December 2021

Contents

1: Introduction

Purpose

The purpose of Technical Bulletins from Audit Scotland's Professional Support is to provide auditors appointed by the Auditor General and Accounts Commission with:

- information on the main technical developments in each sector during the quarter
- information on professional matters during the quarter that are expected to have applicability to the public sector
- summaries of responses to requests from auditors for technical consultations with Professional Support.

Appointed auditors are required by the Code of Audit Practice to pay due regard to Technical Bulletins. The information on technical developments is aimed at highlighting the key points that Professional Support considers auditors in the Scottish public sector require generally to be aware of. It may still be necessary for auditors to read the source material if greater detail is required in the circumstances of a specific audited body. Source material can be accessed by using the hyperlinks. It is also accessible by auditors from the Technical Reference Library on SharePoint* maintained by Professional Support.

Any specific actions that Professional Support recommends that auditors take are highlighted in green.

Technical Bulletins are also published on the Audit Scotland website and therefore are available for audited bodies and other stakeholders to download. However, hyperlinks in this bulletin indicated with an asterisk (*) link to files on SharePoint and are only accessible by auditors.

Highlighted items

Professional Support highlights in the following table a selection of the items in this Technical Bulletin that are of particular importance:

Highlighted items		
Professional Support has published guidance on planning 2021/22 audits [see paragraph 1]	Professional Support has expressed views on some technical consultations with auditors [see paragraphs 4 and 37]	Professional Support has published guidance on risks of misstatement in 2021/22 local government annual accounts [see paragraph 5]

Highlighted items		
CIPFA has issued guidance notes on the 2021/22 accounting code [see paragraph 9]	CIPFA has issued a consultation on proposed changes to the prudential code [see paragraph 12] and treasury management code [see paragraph 28]	The FRC has issued a paper on what makes a good audit [see paragraph 38]
The FRC has issued a report on IAS 37 disclosures [see paragraph 44]	The FRC has issued a factsheet on climate related financial reporting [see paragraph 46]	The FRC has issued a report on Alternative Performance Measures [see paragraph 52]

Contact point

The main contact point for this Technical Bulletin is Paul O'Brien, Senior Manager (Professional Support) – Pobrien@audit-scotland.gov.uk.

2: All sectors

Contact: Paul O’Brien, Pobrien@audit-scotland.gov.uk

Guidance on planning 2021/22 audits

1. Professional Support has issued guidance to assist all appointed auditors in planning their 2021/22 audits of public bodies. The guidance supplements the Code of Audit Practice, and auditors are therefore required to plan their 2021/22 audits in accordance with it. It is accessible by auditors with other supporting materials on SharePoint* but it is also freely available to download from the Audit Scotland website.

2. The guidance covers the main activities that comprise core audit work and the products associated with each activity. It recognises the impact of COVID-19 on completing the 2020/21 audits and the consequent late start to 2021/22 audits, the challenges in performing audits remotely, and the additional complexities and uncertainties involved.

3. The following table provides a summary of the key changes from last year, along with the section of the guidance in which further information is provided:

Nature of change	Relevant chapter
Submission dates for Annual Audit Plans have reverted to pre-COVID dates	1
Rates for additional audit work have been revised	1
Guidance on assessing going concern has been added	2
Target submission dates for audited annual accounts have been moved forward one month from last year	2
Auditors are not asked to carry out any new specific work on the audit dimension areas in addition to their own local risk assessments (with the exception of procurement fraud brought forward from previous years’ planning guidance)	3A
Submission date for Best Value Audit Plans has reverted to pre-COVID dates	3B
Councils where a Best Value Assurance Report is required have been updated	3B
Auditors are required to complete a return to demonstrate when they have reported their audit work on each of the Best Value themes	3B
The removal of the requirement for auditors in local government to consider Strategic Audit Priorities has been extended to 2021/22	3C

Nature of change	Relevant chapter
The removal of the requirement for auditors to contribute to performance audit reports or impact reports has been extended to 2021/22	4
The number of local government grant claims requiring certification has been reduced to two	5E
Guidance has been updated on involvement in the National Fraud Initiative	5K

Technical consultations with auditors

Professional Support responds to requests from auditors for technical consultations

4. The following tables summarise requests from auditors for technical consultations with Professional Support in respect of complex issues arising from the audit of the 2020/21 annual accounts which may apply to public bodies in all sectors, along with the view offered:

How should cloud computing arrangements be accounted for?
Under cloud computing arrangements, public bodies access and use a supplier's underlying software as needed (e.g. through the internet or via a dedicated line). International Financial Reporting Standards (IFRS) do not contain explicit guidance on how a customer should account for cloud computing arrangements and therefore a body needs to use judgement in determining which standard is the most appropriate to apply. In Professional Support's view, the standards most likely to be applicable are: • IAS 17 Leases and Similar Arrangements • IAS 38 Intangible Assets. In determining whether a cloud arrangement contains a lease, bodies should use IFRIC 4 and evaluate whether the arrangement conveys a right for them to control the use of the asset (e.g. underlying servers). The IFRS Interpretations Committee has decided that a right to receive future access to the supplier's infrastructure does not in itself give the customer any rights to control the use of the asset. An intangible asset should be recognised by the body under IAS 38 if: • it controls the software • future economic or service benefits are expected • the body can restrict others' access to those benefits. Where a contract conveys the right simply to access the supplier's software over the contract term, it would not give the body control of the software and therefore it would not create an intangible asset for the body. If the cloud arrangement does not fall within the scope of these standards, it is likely to be a service contract; expenditure would be recognised when the service is received.

The body has not included a senior employee in the Remuneration Report because the individual does not wish to be included. Is this acceptable?

Auditors should presume that information on named individuals will be given in all circumstances. However, the General Data Protection Regulation (Article 21) gives individuals the right to object to disclosure. The employee must give specific reasons, based upon their particular situation, for objecting to the disclosure. Bodies can still make the disclosure if they can demonstrate compelling legitimate grounds for disclosing the information which override the rights of the individual.

Professional Support expressed the following view to the auditor:

- The requirement for public accountability represents compelling legitimate grounds for the required disclosures to be made.
- The body may need to obtain legal advice, particularly if the objection is on the grounds that disclosure would cause the individual substantial damage or distress.
- Where non-disclosure is agreed, the body should instead disclose the fact that certain information has been omitted.

Bodies sometimes enter agreements with employees which attempt to restrict the disclosure of certain remuneration information (e.g. settlement agreements). For the avoidance of doubt, the requirement to disclose information on a relevant individual in the Remuneration Report is not affected by any 'settlement agreement'.

3: Local government sector

Contact: Paul O'Brien, Pobrien@audit-scotland.gov.uk

Technical Guidance Note on risks of misstatement in 2021/22

5. Professional Support has published Technical Guidance Note (TGN) 2021/8(LG) to provide auditors with guidance on risks of misstatement in the 2021/22 annual accounts of local government bodies. The TGN and supporting material is accessible by auditors on SharePoint* and is also freely available to download from the Audit Scotland website.

6. The TGN is intended to inform auditors' judgement when identifying and assessing the risks of material misstatement. The TGN supplements the Code of Audit Practice and auditors are expected to pay it due regard and use it as a primary reference source when performing 2021/22 audits. Auditors should advise Professional Support of any intended departures from the guidance.

7. The TGN comprises a number of modules as summarised in the following table:

Module	Risks of misstatement area	Purpose
Overview	Areas that are pervasive to the financial statements as a whole	Explains the appropriate related accounting treatment and sets out the action auditors should undertake to evaluate whether the body has followed the required treatment
1 - 9	Specific classes of transactions, balances and disclosures in the financial statements.	
10	Audited part of the Remuneration Report	Explains the requirements and sets out the action auditors should undertake
11	Statutory Other Information (e.g. Management Commentary and Annual Governance Statement)	Sets out the procedures for considering the Statutory Other Information
12	Integration joint boards	Provides guidance on the application of the above modules to these specific bodies
13	Pension fund accounts	
14	Section 106 charities	

8. The risks of misstatement for 2021/22 have been updated to reflect new requirements and risks which emerged during the 2020/21 audits that remain applicable. A separate note* summarises the main changes from 2020/21.

2021/22 guidance notes

9. The Chartered Institute of Public Finance and Accountancy (CIPFA) has issued guidance notes* on the 2021/22 Code of Practice on Local Authority Accounting in the UK (the accounting code).

10. The overall aim of the guidance notes is to explain and illustrate how to apply the accounting requirements of the accounting code, provide background to those requirements, and illustrate how they might be applied in practical situations. The guidance is not mandatory.

11. This edition of the guidance notes has been updated to reflect changes to the 2021/22 accounting code (see Technical Bulletin 2021/3 – paragraph 11).

Proposed revisions to prudential code

12. CIPFA has issued a consultation on proposed revisions to the Prudential Code for Capital Finance in Local Authorities. The proposed revisions follow the previous principles-based consultation earlier this year (see Technical Bulletin 2021/1 – paragraph 31).

13. The proposals are intended to strengthen the provisions of the prudential code, primarily in respect of commercial investments. They are briefly explained in the following paragraphs and, in summary, are in respect of:

- borrowing in advance of need
- defining commercial investments
- changes in prudential indicators.

Borrowing in advance of need

14. The current prudential code (paragraph 45) states that local authorities must not borrow more than or in advance of their needs purely in order to profit from the investment of the extra sums borrowed.

15. However, there has been an increasing trend in authorities purchasing property solely to make an investment return. CIPFA is proposing to provide more guidance to assist authorities with their decision making and to underline the importance of the code's provisions in this area.

16. There are therefore proposals to replace the existing paragraph 45 with new paragraphs 49 to 52. This includes:

- Paragraph 50 setting out examples of legitimate prudent borrowing, e.g. financing capital expenditure primarily related to the delivery of a local authority's functions.

- Paragraph 51 stating that an authority must not borrow to invest primarily for financial return.

Commercial investments

17. It is proposed that the prudential code (at paragraph 95) should set out the three categories of investments summarised in the following table:

Category	Definition
Treasury management	Investments that arise from cash flows or treasury risk management activity, and ultimately represent balances which need to be invested until the cash is required for use in the course of business. It may also include: • an allowance for a reasonable level of short-term treasury investments for liquidity purposes • the investment of borrowed cash where it has been prudent to borrow in advance of needing the cash, e.g. in order to reduce financing and interest rate risks.
Service	Investments held primarily and directly for the delivery of public services. There may be financial returns, but they are not the primary purpose of the investment.
Commercial	Investments held primarily for financial return and not linked to treasury management activity or directly part of delivering services. This includes commercial property which is defined at paragraph 91 as any property which the local authority purchases or holds primarily for financial return.

18. The objectives of the prudential code set out at paragraph 1 have been amended to reflect that the risks associated with investments for commercial purposes should be proportionate to the local authority's financial capacity, i.e. that plausible losses could be absorbed in budgets or reserves without unmanageable detriment to local services.

19. Paragraph 53 clarifies that authorities with existing commercial investments (including property) are not required to immediately sell these investments, and that they may invest in the repair, renewal and updating of their existing commercial properties. However, it advises that authorities:

- should review options for exiting their financial investments for commercial purposes in their annual treasury management or investment strategies
- should not take new borrowing if financial investments for commercial purposes can reasonably be realised instead.

20. Additional commentary on the assessment of affordability and the details of risks of undertaking commercial activity within the commercial activities section on determining the capital strategy is proposed to be added to paragraph 24.

Prudential indicators

21. There is a proposal to add new indicators at paragraphs 81 to 85 of the prudential code on the (estimated and actual) net income from commercial and service investments as a proportion of the net revenue stream. This is intended to assess the proportionality of such investments.

22. There is also the option to include a local indicator for net income from commercial and service investments as a proportion of useable revenue reserves.

23. The following changes are proposed to existing definitions:

- Interest and investment income should no longer be netted off finance costs (paragraph 94)
- Clarification is to be added that the net revenue stream should exclude capital grants, contributions and donated assets.

24. There is a proposal (at paragraph 43) that prudential indicators are reported quarterly rather than the current annual basis.

Proposals in earlier consultation not pursued

25. The earlier consultation proposed the addition of a new indicator comparing external debt with the net revenue stream. However, respondents did not agree with the proposal. CIPFA is therefore no longer proposing this indicator, but it will recommend in guidance that local authorities consider introducing this as a local indicator.

26. The earlier consultation also asked for views on the proposal to add an explicit reference to sustainability to the objectives of the prudential code. Respondents were mostly opposed to this on the grounds that:

- it mixed subjective, policy-related issues with the objectivity of the prudential code
- sustainability is a corporate issue which is the responsibility of the senior management team and elected members, rather than directly a finance function.

27. CIPFA is therefore not proposing to add a reference to sustainability to the objectives but instead will provide guidance to support sustainable behaviour (e.g. there is a proposal that paragraph 24 should recommend that the capital strategy explains how capital expenditure is prioritised in relation to the strategic priorities and policies of the authority, such as environmental sustainability).

Proposed revisions to the treasury management code

28. CIPFA has issued a consultation on proposed revisions to the Treasury Management in the Public Services Code of Practice. The proposed revisions follow the previous principles-based consultation earlier this year (see Technical Bulletin 2021/1 – paragraph 34).

29. The proposals are briefly explained in the following paragraphs and in summary are in respect of:

- categories of investments
- environmental, social and governance matters
- a knowledge and skills schedule
- a new liability benchmark.

Categories of investments

30. It is proposed that the treasury management code (at section 8) should set out three categories of investments in line with the proposed revisions to the prudential code (set out in the previous item). There is a proposal to require any service and commercial investments to be categorised into appropriate portfolios reflecting the different purposes, objectives and management arrangements of the investments. For each portfolio, a schedule would be required to set out the investment objectives, and risk management and reporting arrangements.

Environmental, social and governance

31. The earlier consultation proposed a new Treasury Management Practice (TMP 13) to require a body to establish, implement and monitor all arrangements for the identification, management and control of Environmental, Social and Governance (ESG) risks.

32. However, that proposal was not supported by respondents to the consultation. Instead, there is a revised proposal to add a reference that the formal counterparty policy required by TMP 1 should set out the body's policy and practices relating to ESG investment considerations.

Knowledge and skills schedule

33. There is a proposal to add to TMP 10 on training a requirement for a knowledge and skills schedule.

New liability benchmark

34. There is a proposal for a new treasury management indicator for the liability benchmark for local authorities. The liability benchmark is a measure of how well the existing loans portfolio matches the authority's planned borrowing needs.

35. Local authorities would be required to produce the liability benchmark for at least the next three financial years, with a recommendation to do so for at least ten years.

36. The liability benchmark would not be a single measure but would be presented as a chart of the four balances summarised in the following table:

Balance	Explanation
Existing loan debt outstanding	The authority's existing loans which are still outstanding in future years.
Loans Capital Financing Requirement (CFR)	This would be calculated in accordance with the loans CFR definition in the prudential code, and projected into the future based on approved prudential borrowing and planned loan repayments.
Net loans requirement	The authority's gross loan debt, less treasury management investments, at the last financial year end, projected into the future based on its approved prudential borrowing, planned loan repayments and any other forecast major cash flows.
Gross Loans Requirement, i.e. Liability benchmark	This would be the net loans requirement as set out above plus a short-term liquidity allowance.

Technical consultations with auditors

Professional Support responds to requests from auditors for technical consultations

37. The following tables summarise requests from auditors for technical consultations with Professional Support in respect of complex issues arising from the audit of the 2020/21 annual accounts of local government bodies, along with the view offered:

A council has capitalised the salaries of employees working on capital projects. For budgetary reporting reasons, the council has charged the gross salary cost to the Comprehensive Income and Expenditure Statement (CIES) and has credited income equal to the capitalised element. Is this an appropriate treatment?
It is an established principle that internal budgetary reporting should not drive external financial reporting. The council's approach is basically an internal transaction. This is acceptable for internal reporting but not for external financial reporting as it results in an overstatement of both gross expenditure and income in the CIES (although net expenditure is unaffected). For external financial reporting, the charge to the CIES should be the gross salary cost less the capitalised element. The capitalised element should be added to the cost of the asset in the balance sheet. No income should be credited to the CIES. Professional Support advised the auditor that an appropriate resolution would be to make use of the Expenditure and Funding Analysis (EFA). The gross salary cost and internal income should be included in column 1 of the EFA as it is reported internally, but they should be removed in column 2 (as an adjustment) so that they are not included in column 3 (which shows the CIES figures). There is an alternative presentation as paragraph 3.4.2.100 of the accounting code allows additional columns to be added to the EFA so the council could add a column for these adjustments to keep columns 2 solely for statutory adjustments.

A council has capitalised the salaries of employees working on capital projects. For budgetary reporting reasons, the council has charged the gross salary cost to the Comprehensive Income and Expenditure Statement (CIES) and has credited income equal to the capitalised element. Is this an appropriate treatment?

If the council used the EFA, the budgets would have been unaffected and the misstatements in the CIES would have been corrected.

The council revalues its property on a rolling basis every five years. Is that frequency sufficient? What should the council do about assets not revalued at 31 March 2021?

The basic requirement of the accounting code and IAS 16 is that revaluations should be made with sufficient regularity to ensure that the carrying amount at the year-end does not differ materially from the current value.

IAS 16 explains that the frequency of revaluations depends on the significance and volatility of changes in current value:

- Where property experiences significant and volatile changes in current value, an annual revaluation is required.
- Where changes in current value are insignificant, it may be necessary to revalue the property only every three or five years.

IAS 16 allows a class of assets to be revalued on a rolling basis provided revaluation is completed within a short period. The accounting code interprets 'a short period' as meaning that assets are normally measured once every five years for each class of assets. However, this is subject to the condition that the carrying amount does not differ materially from that which would be determined using the current value as at 31 March.

Professional Support provided the auditor with the following view:

- The five-year frequency is a qualified rather than absolute option. It is only appropriate for property which have insignificant changes in current value.
- The council should have determined a valuation frequency based on the expected significance and volatility of changes in current value. This should be informed by the results of previous valuation exercises. However, the frequency should be flexible and respond to changes in circumstances.
- For property not subject to a revaluation exercise at 31 March 2021, the auditor should expect the council to provide evidence that the carrying amount does not differ materially from the current value. It is expected that the evidence would include, as a minimum, a consideration of relevant building indices and changes in the value of comparable assets.

Professional Support advised the auditor to critically examine the evidence and, if judged to be inadequate, request that the council arrange for a valuation of the property be carried out as at 31 March 2021. If the council declined to arrange a valuation, the auditor was advised to consider whether this constituted a limitation of the scope of the audit.

Should Common Good accounts be disclosed as a note or presented as financial statements? Do statutory adjustments apply to Common Good accounts? Do Common Good accounts need specific reference in the Independent Auditor's Report?

The Common Good is an historic managed fund administered by councils in Scotland. Common Good funds fall within Section 106 of the Local Government (Scotland) Act 1973 and therefore are subject to the accounting and auditing requirements of that Act.

As a minimum, Common Good funds are 'other third-party funds administered by the authority' as referred to in paragraph 3.4.4.1 of the accounting code. This would require an indication of the overall nature and amounts to be disclosed in a note to the councils' financial statements. Where the Common Good is a registered charity, a separate statement of accounts is required. The information disclosed in the note to the council's financial statements should be consistent with the separate statement of accounts. It may also be helpful to users if a hyperlink to the statement of accounts is provided.

However, where the Common Good is not a registered charity, it may be appropriate for more information to be provided in the council's financial statements than simply an indication of the overall nature and amounts. LASAAC guidance on accounting for the Common Good recommends that such additional information should take the form of limited financial statements comprising the following:

- A Foreword briefly explaining the purpose and background of the Common Good fund.
- An Income and Expenditure Account and Balance Sheet. Where the council manages several funds, they may be aggregated for financial reporting purposes into the same statement.
- Notes providing information proportionate to the value of the fund.

Where the Common Good is not a registered charity, paragraph 1.3.8 of the accounting code requires it to follow the requirements of the accounting code.

The application of statutory adjustments is set out in the relevant statutory guidance. As the main reason behind statutory adjustments is to mitigate the impact of specified General Fund movements on council tax setting, statutory adjustments do not apply to the Common Good. For example, deprecation on assets is charged to the Common Good without reversal or replacement.

The Common Good accounts are audited by the auditor of the council. Where the information is provided in limited financial statements, an explicit reference to the Common Good accounts should be included in the Independent Auditor's Report in the list of financial statements that have been audited. There is no need for such a reference when the information is disclosed in a note as it will be implicitly included by the overall reference in the model wording to 'the notes to the financial statements'.

4: Professional matters

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Paper on elements of good audit

38. The Financial Reporting Council (FRC) has issued a paper that sets out its views on the key elements of a high-quality audit. The elements are relevant to audit in any sector, including the public sector.

39. The paper recognises that auditing requires the application of judgement within a principles-based framework; it is not just a rules-based compliance exercise. As a result, it is vital for an audit team to not only have the necessary skills and experience, but also the right behaviours and mindset.

40. The FRC defines high-quality audits as those that:

- comply with the spirit and the letter of auditing standards
- are driven by a robust risk assessment
- are supported by rigorous due process and audit evidence
- involve the exercise of professional judgement and professional scepticism
- challenge management effectively
- report unambiguously the auditor's conclusion on the financial statements.

41. The paper discusses the following three key elements in conducting a good audit:

- Risk assessment and planning.
- Execution of the audit.
- Completion and reporting.

42. The following table summarises some key aspects of each element, and provides examples of associated attributes:

Risk assessment and planning

Key aspects	Examples of attributes
Robust risk assessment	Risk assessment procedures should be based on the inherent (i.e. gross) risk. Procedures must take account of the risk of management bias. Audit planning must be appropriately tailored to the risks identified.
Timely planning	Planning must be performed on a timely basis, well in advance of the financial year end. Planning must be led by the appointment lead and include the key members of the audit team. Planning for more complex areas of the audit may involve relevant specialists.
Knowledge and understanding	The audit team's knowledge and understanding of a business must be tailored to the sector and the specific entity. Knowledge needs to be distilled down to the actual audit risks.
Informed expectations	Audit teams must clearly record their informed expectations relating to key financial metrics and performance indicators. The basis for these auditor expectations must be explained and referenced to source material.
Appropriate resources	The audit team must be appropriately resourced at all levels. Auditors need to agree with the entity that sufficient time is provided to enable the audit to the completed to the appropriate standard. More complex risk areas should have responsibility allocated to experienced team members and, where necessary, specialists.
Planning analytical review	Effective planning analytical review blends the team's knowledge and expectations with management information to identify counter-intuitive trends and relationships. The nature of these potential anomalies must be resolved before the start of fieldwork.
Planning the group audit	Auditors must communicate the group audit approach to component auditors.
Communication to those charged with governance	The audit approach must be clearly communicated to those charged with governance. There should be clear documentation of the detailed correspondence and discussion between the audit team, management and those charged with governance.

Execution of the audit

Key aspects	Examples of attributes
Execution of the audit plan	The fieldwork must comprise execution of the agreed audit plan. Audit team should demonstrate how they have applied high-quality judgement to assess the (corroborative and contradictory) evidence they have obtained. The oversight and direction of the work of the audit team is critical. The level of participation of the appointment lead should be greater for more complex, higher risk audits. The audit documentation needs to provide an easy to follow narrative of the audit and the critical thinking of the team members.
Professional scepticism and challenge of management	Professional scepticism may be particularly apparent when assessing management’s judgements and estimates. Auditors must consult appropriately when carrying out the audit of complex areas. Auditors should persist in challenging management if their concerns are not addressed. Auditors are expected to challenge management over whether their narrative reporting is fair, balanced and understandable (and not simply tick off a compliance report).
Specialists and experts	Relevant audit specialists or experts should be brought into the audit team to ensure it has sufficient expertise to assess the risks or to design and perform procedures responsive to the risks.
Group oversight	Better quality audits have particularly close contact with the component audit teams to deal with issues as they arise.
Consultation and oversight	Appropriate consultation with others on complex technical matters is a strength of an audit team. It is essential that those consulted are provided with sufficient information and time. There must be a clear record of the consultation showing how the audit team reached its initial conclusions, how the challenges were dealt with and how any matters arising were subsequently resolved.

Completion and reporting

Key aspects	Examples of attributes
Assess that sufficient, appropriate audit evidence has been obtained	Audit teams should stand-back and assess the level of work performed against the audit plan and ensure that sufficient, appropriate audit evidence has been obtained in support of the conclusions and judgements drawn.
Communicate matters of interest	Auditors must communicate matters of interest to those charged with governance in a timely way. Where teams find themselves in a very time-pressured environment, they must seek to obtain more resource, or delay completion of the audit. If an audit report is delayed, audit teams should record the reasoning.

43. Delivery of the various aspects within these elements depends on a high performing audit practice. The FRC consider that there are six elements to achieving this. These elements are summarised in the following table with examples of some attributes:

Key element	Examples of attributes
Assessing firm quality risks	Early adoption of ISQM (UK) 1 is strongly encouraged as this is expected to lead to improvements in audit quality.
Mindset, culture, governance and leadership	Senior leadership must live and drive the right values, ethics and behaviours that support high audit quality. There must be a clear link between remuneration/promotion and audit quality. Learning from audit inspections (internal and external), including good practice, must be shared across the audit practice and understood.
Performance monitoring and remediation	There needs to be an effective feedback loop to monitor performance of the audit practice; deficiencies identified should trigger decisive corrective action. It is important to create a culture of trust, whereby people are encouraged to openly talk about mistakes and learn from them.
Quality monitoring	Audit providers should re-evaluate the effectiveness of their quality monitoring approach, including hot reviews, and assess how it integrates with the other elements of the quality control system in order to effectively and sustainably remediate recurring deficiencies.

Key element	Examples of attributes
Resources (including recruitment and training)	It is essential that firms have sufficient, suitably trained and experienced staff to service their existing portfolio and support growth plans. Audit firms should align their reward and performance management framework to the delivery of high-quality audits. There should be a consistently applied audit methodology, understood and delivered by appropriately trained people.
Information and communications	Audit providers should regularly communicate with their audit teams and ensure that they have appropriate knowledge and skills. Audit teams should be supported by access to central teams with in-depth knowledge over auditing, accounting and other relevant matters.

Thematic review of IAS 37 disclosures

44. The FRC has issued a report summarising the findings from a thematic review of disclosures related to IAS 37 Provisions, Contingent Liabilities and Contingent Assets. The review considered how effectively a sample of UK companies met the disclosure requirements and provided other relevant information in their 2020/21 annual report and accounts

45. The report set out expected good disclosure for when a matter is material and relevant to the entity’s financial reporting. Good practice in key areas is summarised in the following table:

Area	Explanation
Accounting policies	Concise and entity-specific descriptions of the significant accounting policies adopted in respect of provisions and contingencies
Basis for determining best estimate	Clear and specific descriptions of the nature of each material exposure, the timeframe over which it is expected to crystallise and the basis for determining the best estimate of the outflow
Contingent liabilities	Quantitative information about expected or maximum exposures to contingent liabilities, or a clear and justified statement that it is not practicable to provide an estimate of the financial effect; negative confirmation can be helpful where users may otherwise expect the entity to report an exposure
Indications of uncertainty	Indications of uncertainty in timing and/or amount that help users understand the potential financial effect (which may arise beyond the next financial year) of additional or reduced costs and/or earlier or later timing of outflows

Area	Explanation
Explanation of significant judgement	Explanation of significant judgement exercised by management in determining the recognition and measurement of provisions, setting out the rationale for management's conclusion and the effect on the financial statements of taking an alternative view
Information about critical estimation uncertainty	Quantitative and qualitative information about critical estimation uncertainty affecting the next financial year, including disclosure of key assumptions and sensitivities
Management commentary	Management commentary on significant year end balances and unrecognised exposures, and on significant movements recognised during the period

Factsheet on climate related reporting

46. The FRC has issued a factsheet on the financial reporting of climate-related matters. The factsheet informs preparers of annual accounts about climate-related matters that they may need to consider when preparing financial statements and associated narrative reporting.

47. Although, it is focussed on FRS 102, the principles in the factsheet apply equally to IFRS-based financial statements.

48. The first part of the factsheet outlines the ways in which climate-related matters may impact on a set of financial statements. Although there are no explicit references to climate-related matters in accounting standards, such matters should be considered in the same manner as any other matters which could have a material impact on the financial statements.

49. The guidance in the factsheet sets out the ways in which financial statements should take into account:

- the impact the entity has on climate change (such as investment in carbon-reducing technology)
- the impact climate change has on the entity (such as on the measurement of individual assets or on the long-term viability of the business).

50. Examples of areas where climate-related matters may impact on the financial statements are summarised in the following table:

Area	Examples of impact
Financial instruments	Measurement could be affected if the matters cause credit losses (e.g. through non-payment by borrowers) or impact an entity's ability to obtain finance. The fair value of financial instruments could be impacted.

Area	Examples of impact
Property, plant and equipment	An entity may require to incur expenditure in ways not previously expected or experienced, such as altering existing assets to make machinery 'greener' or to comply with new legislation. Changes in the residual value or useful life of an asset may result from matters such as: • a property being situated in a location expected to be negatively impacted by climate change, such as by rising sea levels • a machine being impacted by changes in legislation designed to reduce dependence on fossil fuels • vehicles becoming obsolete sooner than expected due to rapid technological change.
Provisions and contingencies	Climate-related risks and uncertainties may require the recognition of additional provisions or disclosure of contingent liabilities (e.g. litigation from an increased focus on climate change). A provision for decommissioning an asset may increase if more stringent environmental regulations are put in place, or if the useful life of the asset is reduced (reducing the discount for time value of money).

51. The second part of the factsheet considers narrative reporting. For example:

- Themes included by entities within the narrative reporting should be reflected in the financial statements.
- Entities need to consider the inclusion of climate-related risks in the reporting of their principal risks and uncertainties.

Thematic review of APMs

52. The FRC has issued a report following a thematic review which assesses the quality of the reporting of Alternative Performance Measures (APMs) in UK-listed companies. APMs are indicators of financial performance which involve adjustments to the amounts reported in the financial statements.

53. The review found that, while companies generally provided good quality APM disclosures, their context needs to be better explained, particularly as profit-based APMs tended to be more favourable than their results in the financial statements.

54. The report advises entities to:

- clearly define APMs and explain why they are needed
- ensure that APMs are not presented in ways that give them greater prominence than amounts stemming from the financial statements

- avoid comments that imply APMs have more authority than amounts stemming from the financial statements
- provide specific, tailored explanations for the inclusion of individual APMs
- explain terms such as ‘underlying profit' or 'core operations' and the basis for identifying adjustments as 'non-underlying' or non-core’
- reconcile APMs to the most directly reconcilable line items, subtotals or totals presented in the financial statements.

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Technical developments and emerging risks from October to December 2021

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